MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

HEARINGS

BEFORE THE

COMMITTEE ON BANKING AND CURRENCY

U.S. Congress

HOUSE OF REPRESENTATIVES

SEVENTY-FIFTH CONGRESS
THIRD SESSION
ON

H. R. 7188

(MR. GOLDSBOROUGH)

A BILL TO PROVIDE A NATIONAL MONETARY POLICY WHICH WILL HAVE A DEFINITE RELATIONSHIP TO THE REQUIREMENTS OF DOMESTIC INDUSTRY AND TRADE UNDER THE CONDITIONS IMPOSED BY OUR POWER ECONOMY, WHICH WILL INCREASE PRODUCTION AND CONSUMPTION TO THE LIMIT OF THE COUNTRY'S POWER TO PRODUCE, AND FOR OTHER PURPOSES

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MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, JULY 8, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding. Other members present: Messrs. Goldsborough, Reilly, Hancock, Spence, Farley, Meeks, Ford, Brown, Patman, McKeough, McGranery, Wolcott, Luce, and Crawford.

The Chairman. Gentlemen of the committee, we have met this morning to consider H. R. 7188, the Goldsborough monetary bill.

(The bill referred to is as follows:)

[H. R. 7188, 75th Cong., 1st sess.]

A BILL To provide a national monetary policy which will have a definite relationship to the requirements of domestic industry and trade under the conditions imposed by our power economy, which will increase production and consumption to the limit of the country's power to produce, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE I—COMPENSATED RETAIL PRICES

DECLARATION OF POLICY

Section 1. It is hereby declared to be the policy of Congress to adjust and control the price of commodities sold at retail so as to make it conform to the volume of purchasing power in the hands of the public, and to regulate the purchasing power so that the production of wealth in this country shall be maintained in full measure.

Sec. 2. In pursuance of such policy interbank currency notes are to be issued for financing a discount on prices to consumers at retail, as hereinafter provided.

Sec. 3. As used in this title—

(a) The term "interbank currency notes" means United States currency circulating only within the banking system for the purpose of giving effect to the issue of consumer credits herein provided.

(b) The term "retail discount rates" means a percentage of the current price level of goods sold at retail to be determined by the National Credit Commission as hereinafter provided, and to be published by the Secretary of the Treasury, which discount is to be applied as a discount on the price of goods and services offered by retailers.

(c) The term "compensated price" means the retail price of goods and services after the application of the retail discount, the amount of which discount is reimbursed to the retailer as hereinafter provided.

(d) The term "retailer" means any seller of goods, including dwellings and services, to ultimate consumers who are natural persons, for their individual or family use and not for resale, and also includes service corporations insofar as they supply services at retail to the public for personal or family use.

(e) The term "services" means passenger transportation, distribution to homes of gas and electricity for domestic purposes, rental of homes, hospitalization, schools, and theaters.

(f) The term "national credit" means the amount of national wealth against which money may safely be issued without resulting in inflationary price levels.

(g) The term "national money" means such forms of the circulating medium of exchange that act as purchasing power or are used for the storage of value and includes bank deposits, bank checks, currency, legalized note issues, and coins.

DETERMINATION OF RETAIL DISCOUNT

SEC. 4. (a) Beginning ninety days after the passage of this act the retail discount rate for each month shall be determined by the Federal Credit Commission and proclaimed by the Secretary of the Treasury on the first day of each quarter or at such other times as the Federal Credit Commission shall recommend.

(b) Upon the passage of this Act and until the retail discount rate is determined and proclaimed as above provided, the retail discount rate shall be 15 per centum. Thereafter the retail discount shall be based upon that percentage which the idle productive capacity of the Nation bears to the total productive capacity. The method of arriving at these figures shall conform to the existing practice of establishing index numbers for trade.

(c) No retail discount rate shall be declared unless productive capacity, ascertained as above described, shall exceed consumption by at least 15 per centum. The retail discount rate proclaimed by the Secretary of the Treasury shall be the rate determined by the Federal Credit Commission, except that the rate proclaimed shall not exceed the next preceding rate by a figure of more than 5 per centum. After proclamation of the discount rate the data used in the determination thereof shall be made a matter of public record.

(d) It shall be unlawful for any member or employee of the Federal Credit Commission to disclose the retail discount rate or any information received or employed in connection with the determination of the retail discount rate before said rate shall have been proclaimed by the Secretary of the Treasury. Whoever violates any provision of this subsection shall be dismissed from such membership or employment and shall be punished, upon conviction of such violation, by a fine of not more than $1,000 or imprisonment for not more than one year, or both.

APPLICATION OF RETAIL DISCOUNT RATE

SEC. 5. After the passage of this Act the retail discount shall be applicable to purchases of goods and services from retailers as defined in this Act, made by consumers who are natural persons, for the personal use of the consumer or his family and not for resale, trade, or manufacture. The retail discount shall be paid in the manner prescribed by the regulations of the Secretary of the Treasury, and the disbursals of said retail discount in trade shall be evidenced by suitable vouchers or forms prescribed by the Secretary of the Treasury. As hereinafter provided, said vouchers shall be used in reimbursing the retailer for his disbursal of the retail discount through selling goods or services at the discount price. The intent of this Act is to provide a continuous settlement through the banks to the retailers for the disbursals of the retail discount as provided in section 7 of this title.

CONTRACTS AND REGULATIONS

SEC. 6. (a) No retailer shall be entitled to dispense the discount unless he has applied to the Secretary of the Treasury for, and has received, a certificate of authority or license, and has agreed to conform to all regulations established by the Secretary for the carrying out of the provisions of this Act. The Secretary of the Treasury may suspend or revoke any certificate of authority or license issued by him to any retailer, after reasonable notice and opportunity for hearing to the retailer, upon satisfactory evidence that the said retailer has not conformed to the regulations under which his certificate or license has been issued. An order suspending or revoking the certificate or license issued by the Secretary shall be final and conclusive unless within ninety days after its service the retailer appeals to the circuit court of appeals for the circuit in which he is doing business by filing with the clerk of said court a written petition praying that the order of the Secretary be set aside. Such order shall be stayed pending the disposition of appellate proceedings by the court. The clerk of the court in which such a petition is filed shall immediately cause a copy thereof to be delivered to the Secretary and he shall forthwith prepare, certify, and file in the court a full and accurate transcript of the record in the proceedings held before him under this subsection, the charges, the evidence, and the order suspending or revoking the certificate or license. Upon the filing of the transcript the court shall have jurisdiction to affirm or set aside the order of the Secretary or to direct him to modify his order, and the findings of the Secretary as to the facts, if supported by the weight of evidence, shall be conclusive.

(b) Whoever falsifies any account relating to the issuance of the discount at retail, or the goods pertaining thereto, shall be guilty of a misdemeanor. Whoever by collusion falsifies accounts arising in the costs of production and distribution to the retailers shall be guilty of conspiracy to defraud. Whoever violates any provision of this subsection shall be punished, upon conviction thereof, by a fine of not more than $1,000 or imprisonment for not more than one year, or both.

SETTLEMENT OF DISCOUNT ALLOWANCES THROUGH BANKS

SEC. 7. (a) In order to compensate retailers for their disbursal of the retail discount, all banks in the United States, its Territories, and possessions, engaged in interstate commerce, are hereby authorized and directed to accept all vouchers evidencing disbursal of the retail discount and included in the regular deposits of their customers who hold licenses to disburse the discount, and to honor such vouchers as if they were cash deposits, in the amount of the disbursals evidenced thereby.

(b) Banks entering credits to depositors on account of retail-discount vouchers shall charge them to their interbank currency notes account, and the Secretary of the Treasury, nor his agent, shall deliver to said banks, on request, interbank currency notes to a face value equivalent to the amount of the retail vouchers entered in the books of the bank. Every amount of interbank currency notes delivered to any bank shall be charged by the Treasury to the bank in the books of the Treasury. The liability of the bank to the Treasury thereby set up shall be that of fiduciary and agent for the carrying out of the provisions of this Act, and the banks shall be entitled to make a reasonable service charge to their depositors for the services rendered. The amount of such charge shall be fixed by the Federal Credit Commission.

(c) Retailers' deposit accounts written up by the method herein provided shall be treated by all banks as part of their circulating deposits just as if the write-up had occurred through the discounting of their customers' own notes, and the checks drawn against them shall circulate in the usual manner.

(d) Any person who makes a false entry on a retail discount voucher, or who presents a false retail discount voucher to a bank for deposit, or any retailer who manipulates his sales totals in obtaining settlement of the compensated prices shall be punished, upon conviction thereof by a court of competent jurisdiction, by a fine of not more than $10,000 or by imprisonment for not more than two years, or both, and in addition his license to dispense the discount shall be revoked.

TITLE II—FEDERAL CREDIT COMMISSION

ORGANIZATION OF COMMISSION

SEC. 201. (a) To carry out the purposes of this Act there is hereby created a Federal Credit Commission (referred to in this title as the "Commission"). The Commission shall be composed of seven Commissioners who shall be appointed by the President by and with the advice and consent of the Senate. No person shall be eligible for appointment as Commissioner unless he is a citizen of the United States and in the judgment of the President qualified to develop expert knowledge of economic, industrial, and statistical problems and to perform efficiently the duties required by this Act. Not more than four of the Commissioners shall be members of the same political party. Terms of office of the Commissioners shall expire, as designated by the President, one at the end of each of the first seven years after the passage of this Act. The term of office of a successor shall expire seven years from the date of the expiration of the term for which his predecessor was appointed, except that any Commissioner appointed to fill a vacancy occurring prior to the expiration of the term for which his predecessor was appointed shall be appointed for the remainder of such term. Commissioners shall be eligible for reappointment and shall receive a retiring pension of $2,000 per annum for each year of service, but not in excess of $14,000 per annum.

(b) The President shall annually designate one of the Commissioners to act as Chairman of the Commission. Each Commissioner shall receive a salary of $20,000 per year. No Commissioner shall engage in any other business, vocation, or employment than that of serving as Commissioner.

(c) The Commission shall have authority to employ and fix the compensation of such special experts, examiners, statisticians, clerks, and other employees as it may from time to time find necessary for the proper performance of its duties.

DUTIES OF THE COMMISSION

Sec. 202. (a) There is hereby created an account in the Treasury of the United States to be known as the national credit control account. After the passage of this Act the Commission shall determine annually the value of the unused capacity of industries and people of the United States for the production of wanted goods and services, which amount shall be credited to the national credit control account. Each year the amount in the national credit control account which shall not have been drawn upon in that year shall be written off. The level of values used in determining the amount of the national credit control account shall be the same as in the determination of the retail discount rate. The decisions of the Commission as to the national credit control account shall be final. Said decisions shall be reported by the Commission to the Secretary of the Treasury and said reports shall be used by him as the basis for the establishment and maintenance of the national credit control account.

(b) The Commission shall use all reasonable ways and means to determine the retail discount rate as accurately as possible strictly in accordance with the methods prescribed in section 4 of title I of this Act and without any extraneous influence or advice. The decisions of the Commission as to the retail discount rate shall be final.

(c) The Commission shall establish and maintain a statistical bureau to collect and coordinate the data necessary for carrying out the provisions of this Act and shall be guided in its decisions by the facts disclosed. All statistical departments of the Federal Government shall furnish such aid and information as may be required by the Commission. The Commission shall have authority to call for data and statistics from all economic organizations, trade-associations, and private business which may be required in the judgment of the Commission for carrying out the purposes of this Act.

(d) It shall be the duty of the Commission to fix the service charge for the handling of retail discount vouchers by the banks for their customers as prescribed in this Act.

INTERFERENCE WITH FUNCTIONS OF THE COMMISSION

Sec. 203. (a) It shall be unlawful for any person—

(1) To prevent, or attempt to prevent, by force, intimidation, threat, promise, or in any other manner, any member or employee of the Commission from exercising the functions imposed upon the Commission;

(2) To induce, or attempt to induce, by like means, any such member or employee to make any decisions or order, or to take any action with respect to any matter within the authority of the Commission; or

(3) To induce, or attempt to induce, by like means, any such member or employee to disclose any information whatever except through the channels provided in this Act.

(b) Whoever violates any provision of this section shall be punished, upon conviction of such violation, by a fine of not more than $1,000 or imprisonment for not more than one year, or both.

TITLE III—INTERBANK CURRENCY AND BANK CREDIT CONTROL

Sec. 301. (a) The Secretary of the Treasury is hereby authorized and directed to issue interbank currency notes, through the Federal Reserve System or any other agency designated by him, in such denominations as may be found convenient and in such amounts and at such times as may be required in order to effectuate the provisions of this Act. The total amount of the initial issue of such currency shall not exceed $10,000,000,000.

(b) It is the intent of this Act that the $10,000,000,000 of interbank currency herein provided and such other sums of like nature which may be provided shall constitute a revolving fund for the stabilization of domestic trade by maintaining purchasing power in the hands of the public through adjustment of the retail price level and so as to avoid undue expansion and inflationary conditions.

(c) Such interbank currency notes as may be issued under the provisions of this Act shall be advanced only to the banks and shall be used by them solely as backing for the credits issued to retailers to effectuate the compensated price as provided herein. Thereafter such currency notes shall be received as legal tender throughout the banking system, in the clearing houses, and all correspondents authorized to make interbank settlements but not outside of the banking system.

(d) Interbank currency notes shall be accepted for all forms of Federal taxation payable directly by the banks, and may be used by them as bank reserves, dollar for dollar, but not as a medium for expanding private credit in the form of loans built on fractional reserves.

(e) Upon the findings and advice of the Federal Credit Commission indicating that inflationary conditions are tending to arise, the Secretary of the Treasury is hereby authorized and instructed to recall from the banks such amounts of the interbank currency in their hands as may be necessary to establish and maintain monetary equilibrium.

(f) Upon receipt of said notice the banks shall reduce their outstanding credits so as to increase their surplus reserves sufficiently to permit the return of the proportion of the interbank currency notes held by them to the Treasury without impairing their required legal reserves. In carrying out the provisions of this section the banks shall promote an orderly liquidation and shall not use selective methods which would tend to depreciate any special classes of securities such as those of the Federal, State, and municipal authorities, and the bond and stock markets; except with the concurrence of the Secretary of the Treasury.

(g) Nothing in this Act shall be construed to prevent the use of open-market operations in Government securities or the readjustments of the discount rate by the Federal Reserve banks in maintaining stable conditions in the money market, and nothing in this Act shall be construed to affect the provisions governing the increase or decrease of the required reserves of banks enacted in the Banking Act of 1935, except that the Board of Governors of the Federal Reserve System shall have the power to increase the required reserves of all national and member banks up to and including 100 per centum.

(h) In the event of the banks having to face an emergency demand for currency by depositors beyond their ability to meet without dangerous forced liquidation of their quick assets, said banks may apply to the Secretary of the Treasury for permission to convert interbank currency into national currency notes by presenting the former for exchange. Banks which have availed themselves of this privilege under pressure of circumstances shall proceed with the orderly realization of their reserves and the curtailment of their outstanding credits until they are again able to restore the national currency so borrowed and reestablish the circulating credits previously established by the interbank currency notes held by them.

TITLE IV—GENERAL PROVISIONS

Sec. 401. Any person who violates any of the provisions of this Act shall, in cases where no other punishment is expressly provided in this Act, be punished, upon conviction thereof, by a fine of not more than $1,000 or imprisonment for one year, or both.

Sec. 402. The Secretary of the Treasury is authorized to make such rules and regulations as he may deem necessary to carry out the provisions of this Act.

Sec. 403. There are hereby authorized to be appropriated annually such sums as may be necessary to carry out the provisions of this Act.

Sec. 404. All laws and parts of laws inconsistent or in conflict with the provisions of this Act are hereby repealed to the extent of such inconsistency or conflict.

Sec. 405. If any provision of this Act, or the application thereof to any person or circumstance, is held invalid, the remainder of the Act, and the application of such provision to other persons or circumstances, shall not be affected thereby.

The CHAIRMAN. Mr. Goldsborough will discuss the bill at this meeting.

I want to say that I regard the question which Mr. Goldsborough approaches in this bill as probably the greatest and most far-reaching question before the people of the Nation.

I rejoice at what has been accomplished under the present administration, and at the splendid progress and improvement that have resulted. But I do not think any one who occupies a position of responsibility and who is informed, is entirely satisfied with conditions that exist at this hour. With large numbers of people on relief, with the standard of living enjoyed by a vast majority of the people of the Nation who toil, I think it should be the concern of every man who hold official connection with the Government, and with every citizen solicitous for his country's future, that we should give first thought to the consideration of economic policies, with a view of improving these conditions.

Our resources are unmatched anywhere in the world. The possibilities for happiness and prosperity here are not paralleled among any other people. If only statesmanship and leadership can find a way for our people who want to work, to toil, to produce, and exchange their products in the fullest measure, there is possible for us a happiness of which we have scarcely dreamed.

I believe that the problem of the hour is that of distribution. If we can find a means of exchange and a medium of exchange that will permit the people of the United States to produce within the limits set by one another and a bountiful providence, and exchange their products, we can absorb our unemployment, we can elevate the standard of living, we can face without trembling the public debt of the Nation, and we can find our way into the abundant life which we so much desire, and which I believe a good providence has made possible for the people of this country.

I do not undertake to pass judgment on the technical provisions of the Goldsborough bill; but as to its purpose I am in full accord, and as to the underlying view upon which the measure is drafted, I am in hearty accord.

I believe that somewhere we will find the leadership that will point the way by which we may realize the great producing capacity of the people of the United States, and the method by which they may exchange and enjoy in full measure the products of the soil and of industry. And I think that the key to that problem lies along the lines of monetary policy, as is contemplated in this measure before this committee.

I have labored here for 15 years with Mr. Goldsborough. He has been an ardent, persistent student of this subject, and he deserves great credit for his efforts. I want to ask the members of the committee to attend these hearings, and let us make them instructive and helpful, first to our committee, and then for the benefit of others.

I hope every member who is here this morning will come back to the hearings that will follow, and that other members will find it convenient to be present.

Mr. Goldsborough, we will be very glad to have you address the committee at this time.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. Goldsborough. Mr. Chairman, and my fellow members of the Committee on Banking and Currency, I, of course, am deeply grateful to the chairman for his kind words, and I appreciate very much the presence of distinguished members of the executive departments of this Government and the legislative department of this Government who are gathered here this morning to listen to this discussion.

Heretofore, Mr. Chairman, I have endeavored to discuss this problem of poverty in the midst of plenty along general lines, sociological lines, but I realize the tremendous necessity of endeavoring to correlate anything that is done with the existing monetary system in order to make possible the passage of legislation.

Therefore, this morning I am addressing particularly the banking fraternity, with the hope that the bankers of the country will see in this proposed legislation something that will not only be helpful to them but which will assist them in their endeavor, as public-spirited citizens, to serve their clientele, the people of the United States.

A cursory reading of this bill may give many people the impression that it is just another measure seeking inflation. On the other hand, the more closely it is studied the more I believe it will appear to be based on the known laws that govern the phenomenon of money.

This statement is addressed to the banking fraternity with the hope that it will throw light upon the rationality of the bill itself, and also upon some of the more obscure monetary phenomena. It is a truism to say that the working of our monetary system has been filled with surprises and anomalies even to our best-informed technical bankers. In no other way is it possible to account for the extraordinary experiences we have been through during the past decade.

As a result, much public antagonism has been aroused against the banking profession and many demands have been made that its power be curbed. In fact, a great deal of recent legislation has been aimed at regulating and controlling the issuance of credit through which the bulk of the circulating medium comes into existence as demand bank deposits.

It may, however, be categorically stated that the majority of bankers have been greatly at sea as to the results of their own actions in the issuing of credit to the public, and have been caught in the maelstrom of finance without realizing how it had come about.

The management of a people's money throws terrific responsibility upon those charged with it, and whatever truth there may be in the claim that a sinister money power exists, it is certain that few bankers are conscious of it as a concrete force, driving them whither they would not go, as responsible and public spirited citizens.

The fact is that discarding from this argument any evaluation of the money power to which I have referred, there is sufficient room to study the circumstances which have been largely responsible for our recent experiences, and which lie to a very great degree in the monetary mechanism which we have inherited. At the very outset we are confronted with the fact that gold which many people regard as an anchor to windward of any monetary system is in itself so unstable a commodity that it is constantly creating havoc with the "best laid plans of mice and men" and actually does not hold any industrial system stable. The phase of the gold problem which we are at this moment passing through is sufficient proof of this statement.

What the Nation is concerned with, and what bankers are perforce equally concerned with, and what the bill, H. R. 7188, is concerned with, is to bring about a reasonably sane relationship between a credit system that actuates a power economy based on mass production, and an industrial commonwealth of immense significance to civilization.

As to the philosophy of the bill, the two primary principles upon which the bill is based are: First, money is the medium of exchange which has replaced simple barter and rendered possible the vast complexities involved in the production and distribution of wealth under modern conditions. To be effective it must circulate freely. It cannot circulate freely unless it is available in sufficient quantity to the buyers and consumers who constitute the open market for goods. It is this open market for goods which stimulates production of wealth and the general advance of civilization.

Second, the mechanism by which circulating money gets into the channels of trade is not geared to the consumption production cycle in such a way that an even flow of effective demand for goods can be maintained. The changes that have been wrought in industrial life by the introduction of power resulting in mass production are not being adequately met by the issues of credit solely for the production of goods, and a supplementary source of credit is necessary. The bill is designed to supply this deficiency through a systematized method of price adjustments based upon the relation between the natural demand for consumption of goods and the national ability of our technical equipment and resources to supply those goods.

Both of these statements will be more fully discussed in the following pages in the relation they bear to the banking system. For the present they may be regarded as axiomatic in the light of the experience of the past half century and the statistical history pertaining to it.

The two chief problems that the bill is designed to meet are: First, the proper adjustment of the real value of the monetary unit, the dollar, in its relation to the goods offered for sale. This is something that bankers are greatly concerned with because the majority of bankers are continually harassed by the fluctuation of dollar values; in other words, the dollar itself.

Second, the maintenance of the volume and speed of the circulating medium in relation to its purchasing power and the volume of goods offered for sale. The volume of production should, of course, approach capacity in order to assure profitable operation to industrial plants. It is not a stable money that the bill seeks to establish so much as a reasonably stabilized industrial system. But the one is tied so closely to the other that they constitute essential components.

Both of these problems have held the center of the national stage for close to 10 years. They have become household words amongst us, as "the need for increasing purchasing power" and "the revival of production and employment."

In effect, the bill seeks to establish a "national monetary policy having a definite relationship to the requirements of domestic industry and trade under the conditions imposed by our power economy."

A coordinated national monetary policy has been conspicuously lacking from our national economy both in the banking system itself and in the Federal administration. But it has been recognized as a need and has been called for time and time again. This lack may be explained by the fact that there had appeared no fundamental principle upon which to base one. The machine has now presented that fundamental principle.

The monetary policy that the bill materializes is that it is a Federal responsibility under the Constitution to so adjust the value of money that it conforms to the law of supply and demand. It therefore raises the purchasing power of money by reducing the price of the necessities and comforts of life known as consumers' goods.

Section 2 does this by establishing a general blanket discount on the price level of goods sold at retail. It is done through licenses issued to all retailers to dispense the established discount, by, in effect, selling below cost. In other words, to sell at a discount fixed by a credit commission especially equipped to estimate the current flow of trade. The Secretary of the Treasury is charged with the carrying out of the provisions of the bill and the findings of the Federal Credit Commission which the bill sets up, under rigid statistical restrictions.

The resultant price level of retail goods, which include the public services such as electricity, hospitalization, transportation, and so forth, has the effect of increasing the purchasing power in the hands of the public, arising from whatever source it may, by the amount of the discount. This price level is known as the compensated price, because it compensates for the shortage of buying power as against producible goods.

The retailers who dispense the discount—which means all responsible ones—are reimbursed by the Government through the banking system by means of an issue of interbank national currency, which is not legal tender to the public, but which is used by the banks as a backing for credit and is legal tender within the system.

Under the bill retailers take vouchers from their customers for the discount allowed, which vouchers when included with a cash deposit at a bank by a retailer, are credited as part of his deposit, and charged in the bank's books to its interbank currency account. The bank, in turn, is reimbursed by the Treasury with an equivalent amount of interbank currency notes. The retailer's deposit circulates as he draws checks against it and the interbank currency circulates through the clearing houses in settlement of interbank balances, offsetting the circulating deposits arising in the accounts of the retailers, as the result of the discount. The general level of deposits in the banking system will be increased in exact proportion to the issue of interbank currency and will be lowered correspondingly if or when it is recalled.

The cost to the banks for rendering this service is covered in the bill by a provision for fixing the service charge by the Federal Credit Commission. As far as the banks are concerned the handling of the write-ups of the retailers' accounts to the amount of the vouchers received, it is practically the same as if they discounted a retailer's note, except that instead of charging him interest they make him a service charge and hold interbank currency as the collateral. They get their collateral from the Government, and not from the retailer.

The financial technique involved in the application of the discount at retail will be discussed further in later pages. Suffice it to say here that it should be clearly grasped at the outset, that this issue of credit through an expansion of national interbank currency is so arranged that it only gets into circulation after an actual sale has been consummated. That is the reason I claim it cannot cause any inflation because it does not come into being until it is used for the purpose of creating the distribution of production. In other words, there is always something material, some goods at retail which go to the public when this new money is issued.

Mr. **Ford**. It is a post transaction; is that the idea?

Mr. **Goldsborough**. Yes. It represents actual transactions in trade, increasing the turn-over of the retailers, wholesalers, prime producers, and the transportation systems by the amount of the credit issue, and as much of it as continues to circulate.

Section 3 of the bill is confined to definitions of various technical phrases used in the body of the bill.

Section 4 provides the method for the determination of the rate of the discount at retail which initially is fixed at 15 percent. But thereafter the discount is varied in accordance with the ratio that goods going into consumption bear to productive capacity. A special Federal Credit Commission is charged with this duty. Its duty is to collect and coordinate the indexes of trade, credit, and money in circulation, and to report the findings to the Secretary of the Treasury, who has no leeway to alter their findings. He is charged with announcing the quarterly rate of discount.

The process simply amounts to this, that when wanted goods cannot be sold the retail discount is increased. If demand catches up with supply the discount is cut or discontinued. It is an automatic way of keeping supply and demand in harmony through the price level. A margin of safety is provided in paragraph (c) by prohibiting any discount when the margin between consumption and productive capacity is less than 15 percent.

Sections 5 and 6 provide regulations for the application of the discount. They are administrative and appear sufficiently clear to pass without comment.

Section 7 deals with the settlement of discount allowances through banks.

Some explanation of the technique involved in carrying out the monetary and credit provisions of this bill has already been given. The text of the bill appears fairly specific in these particulars. Anyone familiar with banking methods should readily see that the process of issuing this credit is precisely the same as that of discounting a retail customer's promissory note, except that instead of the note backing the write-up of his deposit account, the credit arises from a deposit of interbank currency by the United States Treasury. This relieves the retail depositor of an obligation to repay, and the bank is protected by the fact that its responsibility is that of a fiduciary. The bank is relieved of the personal responsibility that accompanies the issue of loans on its own account, but all parties are governed by current statistical records.

Title II deals with the organization of the Federal Credit Commission which the bill establishes for the purpose of maintaining a balanced credit system throughout the Nation. Its duties are circumscribed by the statistics of money and trade, which it will collect and interpret. Its specific duty is to maintain a balance between production, consumption, and purchasing power.

It is protected from extraneous political or other influences. Its findings are to be based on the conditions of trade and industry just as the findings of a court of law are based upon the interpretation of existing statutes.

Title III deals with the regulations governing the issuance, circulation, and recall of the interbank currency. From the standpoint of the banker it is the most important part of the bill because it provides the regulations for carrying the terms of the bill through the banking system.

Interbank currency represents a recallable issue of credit which circulates throughout the banking system, in support of discounts on prices of goods and services sold at retail, for the purpose of bringing effective demand into harmony with full production.

It cannot be included as part of a bank's fractional reserves, but it constitutes 100 percent reserve against the credit that has arisen from it. In other words, if a bank has received from the Treasury or a clearing house $100,000 of interbank currency and has $1,100,000,000 deposits, the notes are 100-percent reserve against the odd $100,000 deposits. And as such they circulate everywhere within the system.

As the original credit gets diffused through the circulating deposits of the system the currency becomes equally diffused. Greater activity in the retail trade would call for greater production for replacements, and expanded private production credits. With increasing business security prices would tend upward and the demand for collateral loans would increase.

If a run-away market seemed imminent, the notice of recall of a percentage of notes outstanding would impose upon the banks the obligation of calling in sufficient money to cancel an equivalent amount of credit then outstanding, which would release the notes, in the same way that private collateral would be released, when individual loans are called. And the notes would be returned to the Treasury.

It is not unlikely that this action would result in a lowering of speculative prices, and the consequent added reduction of the loans made for the bank's own account. Normally a movement of this nature, that is, at present, results in a general lowering of trade. But as the retired currency notes were reissued in the form of new retail discounts, the loss of buying power would be offset and demand for goods sustained.

There would be a sound basis for stability and sustained confidence. In other words, the lowering of artificial values on the stock exchange would result in the furnishing of new issues for discount at retail. In effect the system constitutes an alternating current of credit paralleling the alternating current of electricity, now in use.

The introduction of the alternating current is responsible for the benefits we now enjoy from electricity, although its adoption was strongly opposed by people who ought to have known better. At the present time we would be lost without it. An alternating credit system holds as great a potential for the improvement of the industrial and banking world as did this innovation in public utilities.

It is provided that the banks act as fiduciary agents of the Government in the handling of the interbank currency and the credits arising therefrom. For this service a commission is chargeable to their customers at retail, which should offset the loss of income now being experienced by the banks, through the curtailment of trade credits, which was always considered the most legitimate and reliable source of banking income.

Another provision for the protection of the banks is in regard to conversion of deposits into currency on depositors' demand. There is no reason to suppose that the volume of currency in circulation would be increased. In fact, it would probably be reduced as banking activity and confidence would result. Individual banks, however, can always get into trouble, resulting in hasty withdrawals of their depositors' money. Banks thus caught can, on application to the Secretary of the Treasury, convert any interbank currency notes into national currency for their customers. This proviso augments the deposit insurance provisions of the 1935 banking act in the degree that interbank currency notes have increased demand deposits.

Any bank holding these notes can use them for the liquidation of its own Federal taxes. But if it does so it must of course have other surplus resources to support its outstanding credit reserves. It is the design of this bill to establish a fund of permanent bank money that cannot be recalled through a fall in the price level, and that will circulate continuously in the channels of trade. Some of it will constantly accrue to inactive bank accounts through profits and savings. The loss of this money to the blood stream of trade would be replaced automatically under the bill, and if the accumulations of liquid capital became too great it could be called in by any of the means provided or by increased inheritance taxes, which are probably the most wholesome and least objectionable means of taxing the rich.

Paragraph (g), section 301, title III, provides several safeguards against inflationary conditions. It confirms the existing open market operations and rediscount rate control and expands the control of the ratio of fractional reserves by so adjusting the regulations that this element of inflation prevention is established on a sliding-scale basis, the same as the rediscount rate.

The bill, as I have not specifically stated, holds some provision for permitting the Federal Reserve Board to raise the reserve requirements to 100 percent, as was provided in the original 1935 act, as it was introduced in the House.

There are good reasons for feeling that an elastic system of reserve ratios will be a safeguard against the creation of an excess of speculative money.

In this connection it is well to recall certain elements in the situation that culminated in 1929. In the 7 years preceding, a serious credit inflation developed, and bank deposits increased approximately 27 percent from forty-three and four-tenths to fifty-five and threetenths billions of dollars, from 1924 to 1929. Loans increased at the same time over 30 percent, or from thirty-one and five-tenths to forty-two and two-tenths billions of dollars. Those figures are from the Federal Reserve Bulletin.

Other significant statistics are: Commodity price index, 1924, 98; commodity price index, 1928, 97; commodity price index, 1929, 95.

Eligible paper in member banks, June 1926, 4.9 billion dollars; eligible paper in member banks, June 1929, 4.5 billion dollars.

Value of bonds on New York Stock Exchange, Jaunary 1925, 13½ billion dollars; value of bonds on New York Stock Exchange, January 1929, 17½ billion dollars.

Value of stocks on New York Stock Exchange, January 1925, 27 billion dollars; value of stock on New York Stock Exchange, September 1929, 89½ billion dollars.

Commercial loans, national banks, 1924, 8.33 billion dollars; commercial loans, national banks, 1929, 8.12 billion dollars.

Security loans (excluding United States obligations), 1924, 3.64 billion dollars; security loans (excluding United States obligations), 1929, 6.67 billion dollars.

These statistics prove that the inflation that occurred was an inflation of monetized capital values, and that there was not only no inflation in commodities or the cost of living, but that in spite of the plethora of money in the banks and the security markets, the production of consumer goods was not being fully supported.

At the same time that the production index was rising from 100 to 119, the commodity-price index was falling from 98 to 95, the eligible commercial paper was falling from 4.9 billion dollars to 4.5 billion dollars, and commercial loans from 8.33 billion dollars to 8.12 billion dollars.

In these years also technological unemployment appeared and increased, whereby hundreds of thousands of highly trained artisans and experts were unable to earn a living, while the production index climbed 20 percent.

It seems almost superfluous to point out that the apparent overproduction, which was one factor amongst several others that started the downward spiral, was nothing but camouflaged underconsumption.

The question, therefore, of controlling the money of the country so that the capital values that have been created may be justified and inflationary conditions avoided becomes from the bankers' standpoint one of restoring the flow of money through the channels of trade, and not in long-term investment increased capital values.

A NEW TYPE OF CURRENCY

The idea behind this type of currency is the need for increasing the flow of commercial credits which have been the backbone of commercial banks, and out of which the many ramifications of the modern banking system have developed. The volume of commercial credits flowing continuously is one measure of the spendable income of the Nation. It is the savings conserved out of this spendable income that gives solidity to all forms of capital credits, and eventually liquidates them.

If capital values and earnings are to be permanently restored, it can only be through the revival of trade in nondurable goods to a point where debt charges and amortization can be saved out of the flow of new wealth into consumption.

To attain this the ratio of commercial credits will of necessity have to be increased, and so far no way has been found to do this except by Government borrowing and spending and ignoring the threats that inhere to an unbalanced series of budgets.

This statement may be challenged by those who still maintain that private initiative can achieve the same result, and point for proof to the 7 years preceding 1930. But the facts of the case refute any such contention because reference to statistical records shows that while the Federal Government did not at that time borrow and spend beyond its means, the great mass of the active public, and also the minor units of Government, did that very thing. It makes no difference whether the Government or industry follows this route to prosperity, the end is the same, inflation followed by deflation.

Hence the primary purpose of the issue of interbank currency provided in this bill is designed to restore the flow of commercial transactions to a sound ratio with capitalization and capital charges, by injecting into the arteries of trade the ratio of purchasing power that is lacking. It enters the commercial credit stream at such a point and in such a form that every dollar of it inevitably means an immediate increase in trade of that amount.

To repeat, this currency is a limited issue and is designed to circulate throughout the banking system as the backing for the circulating deposits it has given rise to. In this respect it becomes a revolving fund of permanent deposit money for the support of trade. It can only be recalled if or when there appears to be an excess of spendable money over the volume of goods that would cause an unwholesome rise in prices. The Government, under advice of the Credit Commission, would notify banks that they should reduce their outstanding credits so as to establish surplus reserves sufficient to permit the return of the required quantity of notes to the Treasury. The process would parallel the increase of reserve requirements or the sale of Government bonds in open market operations to curtail excess credit.

The bill retains the open-market operations in Federal securities and the control of the rediscount rate as part of a soundly managed credit mechanism, to which the interbank-note issue is added. But the notes have another function which is equally important, that is, to obtain public purchasing power and stabilize the productive income by maintaining the public purchasing power.

It seems unnecessary in this statement to refer to the other administrative and regulatory features of the bill. My main purpose is to try to relate the financial features it proposes to the monetary system as it is, and to show how and why it deserves the support of public-spirited bankers in the interest of profitable banking and a sound monetary system in the public interest.

The origin of money was to facilitate the exchange of goods and services between individuals and groups. The origin of banking was to conserve, protect, and facilitate the transfer of money. As transportation facilities increased and the volume and size of shipments of merchandize expanded, bank credits developed in harmony and provided the medium of exchange that monetized goods in bulk as they passed from hand to hand or place to place.

Without the aid of bankers' credits the growth of the centers of population and group industrialism would have been retarded. The business of banking became profitable and essential. But practically the whole of this financial business was built upon the trade in consumable or semidurable goods. And the credits which established the medium of exchange in them were virtually self-liquidating. They came into existence as goods were produced and transferred and went out of existence as the goods disappeared through consumption, to be reissued for new production.

Metallic tokens of exchange and bullion facilitated these operations on balance, and also as a storage of value. Out of this trade in consumable goods came monetary savings and the growth of material wealth. This trade has been the foundation of banking, finance, and capital as we know it today.

Cooperation between the banking system and the Government is, of course, just as essential in the carrying out of the technique of the bill as it is in other fiscal operations. But by the use of the type of credit expansion provided by the interbank currency notes the banks are relieved of the serious consequences that may follow credit expansion through the discounting of Federal obligations to excess, on the basis of an imaginary market.

The only real wholesale market for Government bonds in the event of a serious credit squeeze is the ability of the Government to issue billions in currency in the process of buying them back. That is generally recognized as the inevitable outcome of the present monetary policies, if continued, and is the essence of disastrous inflation.

On the other hand, the limited currency provided by interbank currency notes is governed in quantity by transactions in trade and throws no strain on the resources of the banks. They would conduct their business as usual, without the danger of forced liquidation, and with an assurance of a demand for goods that would put their industrial customers on to a profitable basis. In other words, the other departments of the business of banking would become increasingly profitable.

And this truth holds good in our time and will continue to hold good under any free economy. The trade in consumption and semidurable goods, and the circulating credits arising therefrom have made sound banking possible, and without them in excess ratio to other forms of finance, such as is involved in the growth of capital, we cannot progress.

I believe this statement will not be denied by any competent banker. It has been asserted time and time again that the recent bank debacle was due to the shortage of these trade credits in relation to general financial conditions that forced the banking system to use its surplus credit for financing long-term obligations. It is certain that the available records furnish ample proof of it.

If we restore our national productive income by means of new long-term credits—which we are now trying to do—and fail at the same time to restore our national spendable income to a parity with them, we face the certainty of greater inflation and greater deflation than we have ever known.

The bill that we are discussing, H. R. 7188, Seventy-fifth Congress, proposes a way to do this, based upon monetary principles which history has proven sound, and which I have tried to outline. In a nutshell it is to restore the flow of trade by restoring the flow of commercial credits through the banking system in such a way as to augment the spendable income and bring it into harmony with our reasonably possible productive income.

Nothing would do so much to give us a sound banking system and profitable capital investments.

In the days when banking consisted chiefly of commercial credits the system of issuing money possessed inherent characteristics that guarded against booms and depressions, except when forced by deliberate Government mismanagement induced by wars, or an occasional speculative boom, like the South Sea Bubble, and other minor ones, in some of which the colonial concessionaires in London and their companies were involved, in the early days of this continent.

The principle underlying the system still persists and may be tersely expressed in the bankers' dictum: "Put money out when prices are rising and pull it in when they fall." In any economy where production is achieved mainly by hand labor, and where large mechanical equipment is not the dominating factor of production, this dictum is "just fine." It follows the provisions of nature.

When nature was lavish and peace prevailed large production needed more money to distribute it. When crops failed and floods and pests were rampant and possible famine threatened, money must be called in to prevent famine prices aggravating the shortcomings of nature.

But these conditions have ceased to exist. The whole system of production and consumption has changed. Power and the machine, plus the vast monetization of capital equipment, has changed it. The worst thing a banker can do now is to start calling in money when prices begin to fall. Carried to excess as it was in 1929 to 1933, few bankers escaped a serious blow, along with the ruin of their friends and neighbors. They were wise in their generation to protect their depositors. They had no alternative. But any system that has that story to tell is obsolete and unsocial under existing conditions.

The reason it is obsolete and destructive to an effective power economy is because science and the machine have made the available supply of goods, both agricultural and durable, a relatively stable item. The volume of merchandise producible is now more a matter of human will than of nature's vagaries. But in order that humanity can gain this control of nature it has been necessary to expand the monetary system in the direction of monetizing capital values and equipment.

The consequence is that unless there is a dependable supply of money available constantly to the buying public the demand for the products of industry, which ought also to be a stable factor, has by force of circumstances become highly unstable. It has become unstable because the supply of money available to it is unstable. The supply of money is unstable because the money issued is based entirely upon the general price level and must be recalled when prices begin to fall.

It was stated previously that in the time when the forces of nature were the chief governing factor of the volume of production the issue and recall of trade credits were a generally stabilizing factor, because a shortage of goods necessitated a reduction in the money supply to prevent the kiting of the cost of living. In those days the great mass of bank credit was issued against goods in trade, which always had been the backbone of sound banking. But in our day the greater part of the credits issued circulate as capital credits, although their validity is based upon the savings arising from the trade in usable goods, which savings liquidate them and provide new capital credits for replacements and improvements.

While bankers still realize the importance of the trade credits to a stable banking system, force of circumstances has driven them into dealing in too great a proportion of capital credits, that is, credits issued against and dependent for their validity upon the earnings of capital. Obviously the earnings of capital are dependent upon the volume of goods passing through consumption, and thus creating replacement demand, continuously and unfailingly. Reliance cannot be placed upon the production of durable goods, because it is so easy to glut the market with them. Demand for durable goods has a narrow horizon compared with the perpetual and necessitous demand for consumable goods.

It would be difficult to glut the markets with consumable goods provided that the purchasing power is adjusted to their volume. It should be clear to anyone familiar with money and banking that if the great mass of capital credits now in existence are to be validated, it must be done through legitimate trade channels; and that these trade channels cannot be supported by credits for capital account.

Recent experience goes to prove this statement.

The R. F. C. has revived at least 5 billion dollars of what was moribund capital credits and in addition the Government has pledged its credit for 15 billion dollars more. The result is an increase of perhaps 25 billion dollars in national income, from 40 billion dollars in 1933 to 65 billion dollars this year.

We have won then, through the capital markets an increase of 25 billion dollars in national income of doubtful dependability by perpetuating and increasing long-term debt to the amount of 20 billion dollars. This is not an encouraging result, in fact there are few bankers who do not regard it as a very dangerous result, especially as another 20 billion dollars will be needed to reach the per capita income of 1929.

We now have about 55 billion dollars of deposits. By that time we would have close to 75 billion dollars. But what use would they be, any more than our 12 billions of gold is useful. Both the deposits and the gold are costly extravagances.

What we need is an adequate flow of trade to validate our capital investments and debts. One-third of the money we have already used to prime the pump would have done the trick if it had been strictly confined to trade channels; in other words, if we had gone back to fundamental banking principles and injected the money into trade channels. On the basis of trade money revolving three times a year, which is a generally accepted economic factor—not to be confused with the velocity of money, which involves the transfer of billions of dollars not related directly to production—one-third of the money we have already used would have inevitably produced the same result. That is, 8 billion dollars revolving three times a year for the purchase of new production would have increased the productive income of the Nation 24 billion dollars, against 25 billion dollars, won by increasing and maintaining long-term debts by three times that amount.

The effect on our whole financial fabric of such a revival of trade would have cured the dry rot that now envelopes the 55 billion dollars of deposits which are moulding from stagnation. Furthermore, it is a pretty safe conclusion that if anything like the 20 billion dollars of new deposits already referred to have to be created in line with our present fiscal policies, a 100-percent reserve will be forced upon the banking system. On the other hand, if trade credits are revived, without recourse to perpetuating the long-term debts as at present, higher reserves than at present may become necessary, but the volume of capital credits can be controlled by open market operations and the rediscount rate, and thus avoid the difficulty that the bankers would be confronted with if the 100-percent reserve were suddenly forced upon them.

The philosophy of the bill we are discussing is that provided the national industry is increased upon a balanced production schedule by maintaining orderly markets through the price of goods, the control of investment, that is, capital credits, will be a matter of intelligent management and the judicious use of the credit expansion safeguards provided in the bill, in the Banking Act of 1935, and in the rules of the S. E. C.

Recent legislation, endorsed by responsible bankers and the public, has been designed to control the get-rich-quick tendencies of humanity and should, in conjunction with the provisions of this bill, provide a monetary system and source of credit for all purposes in ample volume for any justifiable objective.

Dr. Edward Kemmerer was reported as making the following statement in an address before the Pennsylvania Bankers' Association at Atlantic City on May 26 last:

> Probably the outstanding change in American commercial banking during the last half century has been the pronounced shift in banking portfolios from business paper to investment securities. This shift has been particularly pronounced since the World War. For all of our commercial banks in 1915, for example, investments constituted 23 percent of earning assets, and business loans, 40 percent. By 1936 the investment percentage had increased to 60 percent, while the business loan percentage had declined to 19.

This statement bears out the contention on which I have based the main argument of this thesis, namely, that commercial credits are the lifeblood of the financial system and that the flow of money through the channels of trade in sufficient ratio is the only means of validating credits issued against securities.

One of the old rules of banking, which still holds good to a greater degree in Europe, is that commercial credits should always exceed loans on other collateral and investments by 2 to 1. The enormous capitalization of industry which has developed here is responsible for this change and is due to the growth of our power economy.

This change must be offset in some way, so as to bring the source of earnings of industry up to an adequate ratio with our capitalization. It is clearly not sufficient for bankers to rely upon the security markets for validating the capital credits they issue, unless they are assured that the actual earnings accruing to the capital assets they have monetized are maintained in sufficient ratio to assure a reasonably stable market for securities they hold as collateral. And the only way that can be done is to maintain the buying power of the public for goods at retail.

The fact is that there are two types of credit and two separate uses for money, namely, money for moving goods and money for developing capital assets. The second is dependent for its validity on the first. For the most part they are independent of each other and their velocity of circulation differs widely.

They impinge upon each other at certain points in the industrial cycle, but in the main credits issued on capital account through security issues lead an independent life from credits that produce and transfer goods. They impinge upon each other through the price levels, as when new capacity for production is undertaken, or when circulation increases or depresses the commodity price level. But the source of real income and real savings that is the warrant for both types is dependent upon the flow of trade, which is synonymous with trade credits.

Hon. Marriner S. Eccles, at a hearing before the House Committee on Banking and Currency on February 16 last, made the following remark when discussing the proposal to extend the use of Government obligations for collateral security for Federal Reserve notes, which is deemed necessary to guard against a "disastrous inflationary development."

Asked by Representative Ford of California:

> Is not this extension a sort of standby measure—a shotgun in the corner—to be used against a sudden withdrawal of foreign investments?

Mr. Eccles replied:

> Yes; it is available for that purpose, but it is more important for the present position because there is no eligible paper available.

The fundamental credit base of the Federal Reserve System was the adequate flow of eligible paper, in other words, paper arising from trade. According to Dr. Kemmerer, this paper constitutes only somewhat over 20 percent of the outstanding credit in the banks, and it is the only type that is self-liquidating. It must not only liquidate itself, but it must also provide charges necessary to liquidate the other 80 percent, of capital goods credits.

At the present time we are trying to rebuild our financial system on credits issued against long-term debt, although our experience proves that this source of money is ineffective in restoring purchasing power for commodities, except in a minor degree, and at great cost.

In the Formation of Capital, one of the three volumes of studies recently published by the Brookings Institution, Mr. Moulton, the author, says, on page 71:

> The general conclusion reached in this and the preceding chapter, that the growth of capital does not take place unless expansion of consumption is also occurring, does not appear upon close analysis to be surprising. The motivating force in all economic activity, under a system of private initiative, is the wants and demands of the people. The base of the economic pyramid is the production of consumption goods—first, primary necessities, and then comforts and luxuries. In the ascending scale of goods that are relatively indispensable

> we find new plant and equipment at the top. This is because the demand for plant and equipment is derived from the demand for consumption goods which such plant and equipment can produce. A slight shrinkage in the base of the pyramid very nearly eliminates the top.

The conclusion expressed in this quotation bears out the fundamental contention upon which this statement is based. Its intimate relation to a comprehensive monetary system is obvious. Looked at from the financial standpoint it emphasizes the necessity for a free flow of money in the channels of trade which will permit the free flow of goods in harmony with actual demand.

Without reasonable stability in the consumer markets capital credits issued against securities become increasingly dangerous. As they now constitute the greater part of the business of banking, and as the growing demand for capital for technological improvements, and improved housing, continues, it can only be the part of wisdom for the banks, in their own interest, as well as in the general welfare, to see to it that the base of the pyramid is always wide enough to support the superstructure of capital credits.

As the formation of liquid capital has now become the dominent element in banking, there appears no escape from the deductions arrived at here. Dr. Moulton emphasizes this conclusion when he asserts, on page 157:

> The facts show incontrovertably that new capital is constructed on an extensive scale when consumption is expanding rather than when it is contracting.

And on page 158 he says:

> The available evidence also supports the view that the growth of capital is directly related to the demand for consumption goods.

Surely in a capitalistic country like ours, where each young citizen is supposed to carry a capitalist's check-book in his school bag, it would be well to shape our course in the direction that the laws of finance indicate.

In appendix A of Dr. Moulton's book, which I insert, he reviews the analyses of our situation by Dr. Benjamin M. Anderson, E. F. M., Durbin, John A. Hobson, Foster and Catchings, and others.

(The appendix referred to is as follows:)

Table showing long-term and short-term debts, national wealth, and income

[Taken from "The Internal Debts of the United States," Twentieth Century Fund, Inc., pp. 13-301]

	1913-14	1921	1929	1932-33
Long-term debt……billions of dollars..	38	75	126	134
Short-term debt:				
Business debt……do….	47	93	128	89.2
Personal and household……do….	4	9	22	14.4
Total……	89	177	276	237.6
Population……millions..	98	110	121	125
National wealth……billions of dollars..	192	321	385	300
National income……do….	36	66	85	40
Total debt service……do….	2,143	4,953	7,642	7,910
Per capita debt……hundreds of dollars..	387.76	681.82	1,041.32	1,072
Percent of national wealth represented by debts, long-term……	19.7	23.4	32.7	44.7
Percent of national income represented by debt service..	6	7	9	19.8

Mr. GOLDSBOROUGH. On page 181 he summarizes his conclusions as follows:

> The analysis which we have made in America's Capacity to Consume revealing a demand for consumption goods insufficient to call forth the full output of our productive establishment, is not to be regarded as supporting the position of * * * Foster and Catchings. Our analysis did not show that the aggregate disbursements of national income to individuals were less than the prices of goods and services turned out; on the contrary, we contended that they were virtually identical. We were concerned with the allocation of the national income as between savings for investment and expenditure for consumptive purposes, and we showed merely that the proportion of the total income received by individuals which found its way into consumption channels was inadequate to induce full capacity production.

And, on page 184 of the same book, he says:

> The maladjustment between savings and consumptive expenditures did not, as our analysis shows, lead to a proportional expansion of capital goods, and in due course to an excessive output of consumer goods which ultimately broke the commodity markets. On the contrary, the restricted rate of expansion of consumptive demand held the growth of capital in check; while the excess savings wrought havoc in the financial markets.

It is pertinent to this discussion to make one more extract from this important and judicial work, namely, chapter 10, page 136. Under the heading "The disproportionate increase of investment funds," is found the following:

> It was found that in 1929 the savings of the great mass of the population constituted a negligible proportion of the total savings. For example, 59 percent of the population, or 16.2 million families saved in the aggregate only 250 million dollars, while 91 percent of the families, comprising all those with incomes below $5,000 saved only about 4 billion dollars, or a little over 25 percent of the total. On the other hand, 2.3 percent of the families, those with incomes in excess of $10,000, contributed over two-thirds of the entire savings.

Taken together, these three quotations offer a significant explanation of why our banking system finds it hard to meet the conditions imposed upon it by the new production technology. If one eliminates any consideration of controversial doctrines of the various economists, and confines one's self to the realities here presented, it must be clear that the production of new capital must follow the production for consumption. And that the production for consumption must be met by purchasing power adequate to its abilities.

And, as the production of capital is, first and last, a fundamental function of banking, it becomes an essential of successful banking to so order the production for consumption, and the production for permanent wealth in those ratios which will assure a sound money system and a permanent balance between these factors.

It is a recognized truism that 90 percent of the money used in the conduct of business is borrowed money, created and issued by the banking system against supposedly adequate security, and when it is paid off it must be promptly reissued to permit the industrial system to function.

A fact that we all know is that when any commercial credit is canceled it must be promptly replaced with another circulating credit, otherwise the supply of money would soon fail. Even if we conceived of a national economy in which all industry were on a cash-and-carry basis, the accruals of profits and losses would soon upset the balance and the borrowers would have to reappear.

An effort was made in the earlier part of this statement to differentiate between cash credits issued for the purposes of trade and those issued against capitalized values as monetary and economic factors. In a smoothly working production-consumption cycle trade credits are practically automatic in their functions. But there are many economic and psychological factors entering into the creation and repayment of long-term debt. The subject is too complex to discuss adequately here and now. I must confine myself to the repetition of the statement that the amortization of long-term debt is a function of the volume of credits in trade from which real profits and savings evolve.

Maintenance of long-term debt within the limits of our earnings to meet its charges is one of the greatest problems of the banking system, another being the maintenance of adequate purchasing power to validate our investments of productive capital.

A comparatively recently recognized monetary phenomenon is the growth of long-term debt in excess of the increase in production of real wealth measured in real dollars. As appendix A of this statement, there is a copy of the summary of Evans Clarke and associates sponsored by the Twentieth Century Fund.

It shows an increase of long-term debt between 1921 and 1932 from $65,000,000,000 to $134,000,000,000. If we add the increase of Federal debt we get for 1936 upward of $154,000,000,000. At the same time business debts fluctuated between $93,000,000,000 in 1921 to $128,000,000,000 in 1929 and $89,000,000,000 in 1932–33.

In view of the fact that the economic base of this pyramid, namely, national productive income, rose between 1921 and 1929 from about $65,000,000,000 to $85,000,000,000 and then fell below $40,000,000,000, it is easy to see why the forced liquidation of the early thirties failed to clear up the financial situation and left the banking system virtually bankrupt. The fact is that the country has been living off of the fixed capital that it has monetized for several years past. First, that monetized by the banking system; and, later, that which the Federal Government in partnership with the banks had monetized through increasing the Federal debt.

This persistent increase of long-term indebtedness is an economic phenomenon that is comparatively new. It is inherent of the growth of the machine age and power production. It is due to the need for vast amounts of new capital, which cannot be adequately amortized within the life of the values that gave it birth.

This statement would not be complete without some reference to the pressing problems of balanced budgets and taxation.

When I addressed the House on June 8 last, I stated that our tax rate from all governmental units is the second highest of those countries whose records are available. Great Britain only takes precedence of us. But in spite of this, our national budget is further out of balance, and the only way to balance our budget and pay our taxes is to increase our productive income.

I said then:

> The income of the people of the United States is now about 65 billion dollars a year. That income, by operation of the legislation I suggest could be increased as gradually as necessary to 100 billion dollars in at least 18 months.

What would be the result of that increase? The percentage now of taxes in relation to income is about 6½ percent, yielding now about 4¼ billion dollars. Without increasing the percentage of taxation on an income of 100 billion dollars a year we could raise 6½ billion dollars in taxation. By introducing that other 35 billion dollars of wealth we would be able to release from relief and from governmental support about 2 billion dollars of labor and services. In other words, the Federal Government would be relieved of about 2 billion dollars of pressure that is now brought upon it, so that by increasing the National income to 100 billion dollars you could balance the budget and begin to pay off nearly 4 billion dollars a year of National debt.

It may be well to point out here that a national income of 100 billion dollars a year would be just about equivalent to the per capita income of 1929, allowing for the increase of population. Also the increase of income of 35 billion dollars which I referred to as the introduction of new wealth, means, under the operation of this bill, not inflationary money .

The money provided is limited to 10 billion dollars. The warrant for it comes from exactly the same source as any other type of trade credit; namely, the production and distribution of goods, because none of the 10 billion dollars is available except as it creates and distributes goods.

While it cannot be said how much of this fund would be needed, there is good ground for the assumption that it would be less than the full amount provided, because it would bring about trade activity now dormant and tend to encourage the flow of credit through the normal channels of banking and commerce.

The point is that it would be an antidote to the otherwise inevitable growth of long-term debt which is now out of all proportion to the fundamental credit base of the economic pyramid.

In this statement I have tried to outline some of the basic financial problems of today, and to clarify the means by which this piece of legislation, H. R. 7188, proposes to meet them.

A necessary part of the work of industrial engineers and executives is to study and adjust their so-called production flow sheets to the advances in techniques. H. R. 7188 visualizes a financial flow sheet to meet the needs of the flow sheets of industry and trade.

Every good industrialist knows that if he can so order his plant that he can raise wages and at the same time lower prices he is on the road to success. Every retailer knows that lowering prices stimulates sales. The railroads have recently learned the same thing. No system that does not take into account the relation of dollars to goods at the base of the economic pyramid will succeed, and, as far as I have been able to learn, this bill is the only coordinated attempt to do this thing without disturbing our social order in one way or another.

It does not solve all social and labor problems. But I hope it lays a stable foundation for their orderly solution. It is not a panacea; it simply follows the dictates of technological advance throughout the world with a careful heed to realities.

The choice of our times lies between democracy, dictatorship of the proletariat, or dictatorship of the autocrats. A few years more of our present course will land us with one or the other or, still more probably, in a maelstrom of both.

(The appendix above referred to is as follows:)

Table showing long-term debt, short-term debt, national wealth, and income

Classes	1913-14	1921	1929	1932-33
Long term debt .... billions of dollars	38	75	126	134
Short term debit:				
Business, etc .... do	47	93	128	89
Personal and household .... do	4	9	22	14
Total .... do	89	177	276	237
Index industrial production, Federal Reserve Board, 1923-25=100		85	119	64
Wholesale commodity price—Index 1936=100	68	97	95	65
National wealth .... billions of dollars	192	321	385	300
National income .... do	36	66	85	40
Total debt service	2.14	4.95	7.64	7.91
Per capita debt .... hundreds of dollars	387	681	1,041.32	1,072
Percent of national wealth represented by debt	19.7	23.4	32.7	44.7
Percent of national income represented by debt service	6	7	7	9
Population .... millions	98	110	121	125

Mr. Goldsborough. Now, gentlemen of the committee, it is not my claim, of course, that this bill as it stands should be reported by the committee and passed by the Congress. It is my hope that it may be available to be used as a basis for the formation of legislation which will solve our national problem; that is, our fundamental national problem, the problem of poverty in the midst of plenty, the problem of our inability to distribute to our people all of the wanted goods and services which the same people are able to produce.

Now, with that idea in view, I do ask of this committee and of those appearing before this committee—I have no reason to doubt that it will be done; I have every reason to believe that, so far as the committee is concerned, knowing the members of the committee as I do, that it will be done—that the bill be considered sympathetically; that is, if the provisions of the bill are not what they should be, that the problem of balancing production with consumption be carefully kept in the minds of the committee, so that when the committee undertakes to criticize this measure constructively, or any part of it, they may have something to offer as a substitute, so that we may get somewhere in this discussion toward a solution of the problem.

The executive departments of this Government, the Treasury Department, the Federal Reserve Board, the Federal Deposit Insurance Corporation, the great bankers of the country and their economists, can throw a tremendous light upon this situation if they will endeavor to do so.

My own opinion is that the problem has become one of such interest that the executive departments of the Government and the great bankers of the country and their economists will lend such assistance as they can to this committee for the purpose, not of passing this bill, but for the purpose of solving this problem. And, as far as I know, as far as I am aware, this bill is the only measure before any legislative body in the world that has for its purpose an attempt to solve that problem.

Gentlemen of the committee, it is now 12 o'clock and I have an engagement to go to Salisbury, where I am to speak this evening, and I have to leave at half past 12 o'clock.

The CHAIRMAN. Mr. Goldsborough, we would be glad to have you resume your testimony, if you desire to pursue it further, when the committee meets again.

This committee will meet tomorrow morning at 10:30 o'clock, and will continue the discussion of your bill, if you desire. Or, if you wish to be away for several days, we have other business before the committee, so that we can use the time tomorrow to advantage.

Mr. PATMAN. Mr. Chairman, I desire to ask Mr. Goldsborough some questions, and I would like to have plenty of time to do it.

I congratulate the gentleman from Maryland on his very fine and instructive address. It was very interesting, and I want to ask him some questions about his bill.

The CHAIRMAN. Of course, we will give everyone an opportunity to propound questions and to discuss the matter fully.

I want to thank you, Mr. Goldsborough, on behalf of the committee, for your address this morning. I am very sure it has been fully appreciated.

Mr. FORD. May I ask one question? As to this credit money that is going to circulate between the banks, could you tell us in a few words, on what that is based?

Mr. GOLDSBOROUGH. It is based on the goods which they produce.

Mr. FORD. In other words, it will be the same kind of money I would get from a bank if I had 100 automobiles that I produced and wanted the capital to move them?

Mr. GOLDSBOROUGH. That is correct.

Mr. FORD. That is what I wanted to get at.

The CHAIRMAN. If you cannot be with us tomorrow, Mr. Goldsborough, we can go ahead on something else.

Mr. GOLDSBOROUGH. There are other gentlemen who are going to appear before the committee, but who wanted to hear my statement before they were in a position to discuss the subject before the committee. I will probably not be able to return until next Tuesday.

The CHAIRMAN. We have some other matters to consider, and we will resume the discussion of your bill next week—probably on Tuesday.

Without objection, the committee will now stand adjourned until tomorrow morning at 10:30 o'clock.

(Thereupon the committee adjourned to meet tomorrow, Friday, July 9, 1937, at 10:30 a. m.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

TUESDAY, JULY 13, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m. to give further consideration to H. R. 7188, Hon. Henry B. Steagall (chairman) presiding. Other members present: Messrs. Goldsborough, Reilly, Hancock, Williams, Spence, Farley, Ford, Brown, Patman, Transue, McGranery, Wolcott, Luce, and Crawford.

The **Chairman.** The committee will be in order, please.

Mr. Goldsborough, I understand that you are ready to resume your discussion of H. R. 7188. We shall be glad to have you proceed.

Mr. **Ford.** Mr. Chairman, I have a question——

Mr. **Patman.** I asked the privilege of asking him some questions the other day.

The **Chairman.** Mr. Goldsborough is here to answer any questions that the members may wish to propound.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. **Goldsborough.** I had completed my statement, but Mr. Patman had said that he would like to ask some questions, and that is the reason I am here again.

Mr. **Ford.** I have a question.

The **Chairman.** I will recognize you, Mr. Ford.

Mr. **Ford.** Would you mind elaborating on this discount, and tell just exactly what its relation is to a business transaction, and also what this interbank money is?

Maybe I do not make myself clear. In your statement, very excellent statement, very beautifully phrased, and, I thought, very logical up to that one point, you referred to this interbank money, but I do not know just what you mean by that, what that money is. It is a separate and distinct money, as I get it, that is going to circulate among the banks only. For instance, I have 100 automobiles that I want to sell for $1,000 apiece. That is $100,000. But when I come to sell them, I find that I cannot sell them at that price, and so I do sell them at $850 apiece, leaving a 15 percent shortage. So I sell them for $850 each, or $85,000. Then I go to my bank and take to the bank the certificates from the people who bought them, and I am $15,000 short, and the bank gives me credit on its books for that $15,000—is that the idea?

Mr. **Goldsborough**. That is correct, sir. Of course, you are bearing carefully in mind, I am sure, that these automobiles are sold to the ultimate consumers only.

Mr. **Ford**. I understand, but I have the ultimate consumers' certificates. In each case the ultimate consumer paid $850 for a $1,000 machine.

Then, as I understand it, the bank takes those certificates and sends them to the Treasury, but the bank will give me credit on its books for that $15,000. Where did that $15,000 come from?

Mr. **Goldsborough**. Well, now, I want to answer your question, but I think that I can do it more satisfactorily by asking you a question. Might I ask you what your conception is of where a bank's money comes from when you check on an account?

Mr. **Ford**. I will answer your question by putting myself in the postion of a borrower from the bank. We will say that I am a manufacturer, and I have in process of manufacture $20,000 worth of goods. I find that my cash resources are such that it is necessary for me to borrow from the bank $8,500 to carry that out.

Mr. **Goldsborough**. Had you not better borrow $10,000, in order to carry out the logic of what you have to say?

Mr. **Ford**. No; because I have some cash resources. My material account, my labor account, and the general overhead I am taking care of, but in order to carry out that transaction I borrow $8,500 from my bank. My idea——

Mr. **Goldsborough**. May I proceed from there, because I think that I can carry it so that I can answer you?

Mr. **Ford**. I want to get your idea.

Mr. **Goldsborough**. Yes. Let us assume that instead of you borrowing $8,500 you have $8,500 and you borrow $1,500, and you deposit that in either that bank or some other bank. It goes into the banking system and that puts $1,500 in circulation, and that $1,500 is backed either by the collateral you put up, or, if it is a character loan, where there may be no specific collateral, but you are supposed to be good for $1,500.

Now, that money has no material existence; it is not a thing that you can put your finger on at all; it is simply created by a bookkeeping process, and it is created on the theory—and this is the bank's theory—that there are goods which it represents, and that is the banking justification for it—that it is matched by something material, and that therefore it is not inflationary.

Well, now, this money which is provided for in this bill is that same kind of money, but it comes into actual being when it is matched by goods which are purchased by that money and when the goods go into consumption.

Mr. **Ford**. It is a post transaction, when those goods have gone into consumption?

Mr. **Goldsborough**. No. The theory of this bill is that that 15 percent would never have gone into consumption except for the lowered price, and that therefore it is not inflationary—that this 15 percent is matched by the goods which it makes possible. The Federal Credit Commission—and that happens to be the name that we have given to the organization in the bill—is simply a creation of the bill, and it has a book, and on that book is written 10 billion dollars, but none of that 10 billion dollars is used except as it is matched by goods which go into consumption, none of it.

Mr. FORD. Now, Mr. Goldsborough——

Mr. GOLDSBOROUGH. Does that answer that part of your question?

Mr. FORD. No; it does not, Mr. Goldsborough, for this reason—and we are trying to get this thing out in the open, of course; you understand my motive.

Mr. GOLDSBOROUGH. Of course.

Mr. FORD. In the first place, the man who is borrowing the money—the money to create the goods, pay labor, and buy material—is actually bringing into production something that has value.

Mr. GOLDSBOROUGH. That is true.

Mr. FORD. Under your plan, as the thing has been brought into existence, it has been fixed as to value, but we find that for some unaccountable reason it does not sell, and therefore, in order to sell, we cut the price.

Mr. GOLDSBOROUGH. No; that is not the conception, Mr. Ford. Of course, the conception is that the goods would not be produced except for this 15-percent discount, and the reason that they would not be produced is because the potential producer would say, "There is no use of my producing this 15 percent of goods, because I cannot sell them," and therefore the ultimate answer to your question is evidently that this 15 percent enables the production of goods which would not otherwise be created, and it would not be created because there would be no market for it.

Mr. FORD. Let me say this in connection with that: Regardless of what character of product I am a manufacturer of, if I felt that I could go around and do that, and always be sure that if the market slowed down I could get help from some funds that would take care of any losses that I might ultimately accrue from my operations, why wouldn't the manufacturer go out and just produce goods ad infinitum, with the understanding that he could just go to the bank and get the difference between what they cost him and what he could sell them for?

Mr. GOLDSBOROUGH. The answer to that, it seems to me, is this: That it would be a blessed thing if our people had the means of getting wanted goods and services, and it would not make any difference to me, and I do not see how it could be an economic evil, to have a condition where the people were able to procure all the wanted goods that they were able to manufacture.

Mr. FORD. I would love to see that, and your objectives, I will say, are as near ideal and desirable as anything could be, but I am just wondering whether or not the method you have devised for taking care of it is a method that would work. I am not worrying about its soundness, or anything of that kind.

Mr. GOLDSBOROUGH. I do not know of any other method myself. I have thought about it a lot and investigated it a lot. I was thinking this morning before I got up of something that I might be asked, and this occurred to me: Let us suppose that in 1930, when this depression started, that instead of the various devices which have been used we had simply created a system where retail prices could be reduced to a point where people could buy the goods. That of itself would have put an end to the depression in a very short time.

Mr. **Ford**. I do not think it would, for the reason that——

Mr. **Goldsborough**. It would have started production, and when you do that, you have done it all. As soon as you start the production of consumption goods, you create a revolving fund of money, and it is the answer to the whole problem.

Mr. **Ford**. That would be true if it were not for some extraneous factors, and there are several of them. I think that if we were concerned only with production, distribution, and consumption, that would be true, but we are living in a system where there are several other factors that enter, and I wish to the good Lord that I could see it, for I have in the last couple days put 7 or 8 hours of the most intensive thinking that I know how to do on it, because the objectives, as I say, are very desirable, and I wish that I could work this thing out in my own mind and convince myself that you are right, that we have probably got hold of a solution to our present-day problem, but frankly the post result of it, and I mean by that that it comes in secondarily, I just cannot see. I wish I could.

Mr. Patman wants to ask you a question, but I just wanted to try to get this thing into my mind, and I am sympathetic with you, and, Lord, I would vote for your idea 1,000 percent if I thought that it was the solution. But you, like everybody else, know that one single plan can never be the solution for any great problem. The objectives that you have in mind, and the methods by which you propose to carry them out I think might possibly be a great help in solving our problem, but there is one thing that sticks in my mind and that is that this money is, as you say, the same money that the other kind of a loan creates. If I could see that, it would help. Maybe if we sat down privately, you might get it into my head.

Mr. **Goldsborough**. In the one case, in the case of a loan from a bank to the retailer, he has that money to repay, of course. That money is supported, for the purposes of this statement, by the collateral which he puts up. In the other case—that is, in the case of money created by this plan—the collateral consists of goods, the production of which is made possible by the discount.

Mr. **Ford**. Don't you mean the reproduction?

Mr. **Goldsborough**. No. I mean this, that it is evident to my mind—and that may be the point where our minds diverge, that this is the case: In my conception, a reduction in price of 15 percent, for instance, if that happens to be the discount that is in vogue, would be matched by an increased production of 15 percent. That may be where we diverge.

Mr. **Ford**. I think it is. I think you hit the nail on the head, because your theory is that since these 10 automobiles were sold, that theoretically there is room for 10 more?

Mr. **Goldsborough**. No; my idea is this, that if under this plan it would be possible to sell 10 automobiles, that without this plan it would only be possible to sell eight and a half.

Mr. **Patman**. I have some questions to ask, Mr. Chairman.

The **Chairman**. Mr. Patman.

Mr. **Patman**. Mr. Goldsborough, you know Maj. C. H. Douglass, do you not?

Mr. **Goldsborough**. I met him at Senator Cutting's several years ago.

Mr. **Patman.** When we were out there together?

Mr. **Goldsborough.** Yes; that is the only time I have ever met him.

Mr. **Patman.** You are acquainted with his plan of national dividends?

Mr. **Goldsborough.** Well, I do not know that I can answer that categorically, and I will tell you why——

Mr. **Patman.** Does not your plan——

Mr. **Goldsborough.** Will you let me finish, please?

I have read all of the literature which emanates from whatever his theory may be, but his writings to me are obscure, and his statement at Senator Cutting's was very obscure. I did not understand it at all. I asked him that night——

Mr. **Patman.** I was——

Mr. **Goldsborough.** I asked him specifically that night, because I did not understand exactly what he was driving at, and I thought that maybe I could gather it by asking what his remedy would be, in other words, what his bill would be, what his legislation would be, and his answer was, "I would have to leave that to statesmen."

Mr. **Patman.** But he did advocate one specific thing, did he not, and that was the lowering of retail prices?

Mr. **Goldsborough.** I do not remember that he did at that time, but that is what his works seem to indicate, that technological advances are such that it is impossible to get into circulation to the masses of the people who labor anything like all of the fruits of that labor, and that therefore it is necessary to supplement them by a discount of price.

Mr. **Patman.** Subsidies to reduce prices, he called them, and he advocated a 15-percent reduction, did he not, the same as is provided for in your bill here?

Mr. **Goldsborough.** Not that I know of.

Mr. **Patman.** Do you know how your plan differs from his plan on that?

Mr. **Goldsborough.** As I told you, Mr. Patman, on that night he did not submit any plan, and as far as I know, in none of his books does he submit any plan at all.

Mr. **Patman.** I have his books, and he advanced a plan exactly like yours, and he says that he is advocating that because he wants to reduce the price level.

Mr. **Goldsborough.** I may be mistaken, Mr. Patman, but if he has ever originated any plan except the plan for Scotland, which he has in a supplement to one of his books, I do not know what it is. If he has any other plan, I have never seen it, and I think that I have read everything that he has written.

Mr. **Patman.** There is one paragraph in one of his speeches that he made in which, after he discusses subsidies to reduce prices——

Mr. **Goldsborough.** Do you mean in one of his books?

Mr. **Patman.** Yes; in one of his pamphlets.

Mr. **Goldsborough.** How recently?

Mr. **Patman.** 1936—it is February 14, 1935.

Mr. **Goldsborough.** He got that from the bill which I introduced in September 1935.

Mr. **Patman.** He speaks of it on February 14, 1935.

Mr. **Goldsborough.** 1936. I understood you to say.

Mr. **Patman**. I thought it was 1936, but I looked at the back of the book, and it shows February 14, 1935.

Mr. **Goldsborough**. I have not read that speech.

Mr. **Patman**. Here is what he says, after discussing a plan that I consider to be identical with your own:

> We propose to apply a certain proportion of the total created money to a reduction of prices. The public itself will pay part of the price out of their own pockets in the ordinary way, and a part of the price will be paid by various means through the creation of national credit. The effect will be a drop in the price level, while at the same time the producer and the businessman will not be losing money. They will enjoy the dividends and increase of trade which come from the ability to charge lower prices without losing money as they would if they had the lower prices without the creation of national credit.

Mr. **Goldsborough**. You spoke of a bill that he has formulated.

Mr. **Patman**. I did not mean to say that. I am just telling you what he has advocated. I do not have any knowledge of any particular bill, but after talking with him over at Senator Owens' and after reading all of his different books and pamphlets, I am convinced that what he is advocating is for the purpose of lowering prices. He seems to think that the lower you make prices the more will be consumed, and in that way everybody will be helped.

Well, of course, as I told him that night, I do not agree with him, because I think you have to have good prices in order to get good wages, and where you have low prices you have low wages.

Now, to get to this proposal of yours, as I understand it, every retailer in this Nation—and there are about 1,550,000—would have first to get a license, would they not?

Mr. **Goldsborough**. Yes.

Mr. **Patman**. They would get that license from the Federal Government, the Secretary of the Treasury, and when they receive that license they must obligate themselves to comply with certain rules and regulations laid down by the Secretary of the Treasury; is that right?

Mr. **Goldsborough**. That is right, and the rules and regulations under this bill will be laid down by what is known as the Federal Credit Commission, and the licenses would be obtained under this bill from the Federal Trade Commission.

Mr. **Patman**. Yes; so that all would be licensed.

Now, suppose that a farmer sells eggs and produce directly to the consumers. Let us suppose that the farmer has been selling eggs to you. He would come to you, but you would say, "You are selling them for 40 cents a dozen, and I can get a 15-percent discount from the store. I cannot afford to buy them from you because you cannot give me a discount. You are not a retailer under this law. You do not have a license."

Therefore, that farmer would have to reduce his price, would he not?

Mr. **Goldsborough**. No.

Mr. **Patman**. Why would he not have to reduce his price to meet that competition, if you could buy them for 15 percent less from a recognized retailer who had a license than you could buy them directly from the producer or farmer? The farmer would certainly have to reduce his price to meet that competition.

Mr. **Goldsborough**. I do not agree with you, and I will explain why. The answer to that is this, that the farmer is essentially not a retailer. Essentially he is a prime producer. Now, if you can increase the sale of eggs retail, and if you can reduce the price of eggs from 20 cents a dozen, I will say, to 15 cents a dozen, the retailer who sells the eggs will sell 25 percent more eggs, approximately, than he would otherwise do, and the farmer would have a 25 percent greater market for his eggs than he would otherwise have. As soon as you can increase sales by retailers you will immediately increase sales by wholesalers to retailers and sales by prime producers to wholesalers or to retailers, as the case may be, so that if you can get your retail machinery working faster, it increases to the same extent the machinery of every businessman who is behind the retailer, because the retailer has got to get his stuff either from the wholesaler, manufacturer, or the prime producer.

Mr. **Patman**. I believe that it is logical to assume that one who did not have a license to sell, if he had anything to sell, would have to reduce his price 15 percent to meet the competition of the store that was licensed and that could sell for 15 percent under. That is right, is it not?

Mr. **Goldsborough**. Well, it might be possible, of course, to conceive of an individual case, but in my opinion if a better market, an improved market, were given to the retailer, it would certainly get through to the business behind the retailer. Some farmer, instead of taking his eggs to the store, as he naturally would do, might go around to some housekeeper and ask her to buy eggs from him, but he would be a very foolish man if he did it, because he could get full price for his eggs at the store and he would be bound, if he carried them to the housewife, in order to get a market, to reduce his price by the discount of 15 percent. So the sensible thing for him to do is to take his eggs to the store, and that is what they would do, anyhow.

Mr. **Patman**. Would not that be freezing the channels of trade to the extent that people would be forced to do business with retailers, those who had anything to sell, and those who had anything to buy would go to the retailer, and that would force through that bottleneck, the retailers, all business done by the consumers, for the reason that the growers otherwise could not afford to deal directly with the consumers.

Mr. **Goldsborough**. They do not, anyhow.

Mr. **Patman**. I thought they did in a great many sections. I am sure that they do in my section.

Mr. **Goldsborough**. If they do, I do not know it.

Mr. **Patman**. But, anyway, the licensed dealer under this law would have every advantage, would he not?

Mr. **Goldsborough**. No.

Mr. **Patman**. He would not have?

Mr. **Goldsborough**. No. He would not have any greater advantage than the farmer would have, for that advantage would get back to the farmer in 2 or 3 days.

Mr. **Patman**. This bill says that the term "retailer" means any seller of goods, including dwellings and services. What does "dwellings" mean? A home, a house, and everything connected with it?

Mr. **Goldsborough**. Yes.

Mr. **Patman**. Like a refrigerator, and everything connected with it?

Mr. **Goldsborough**. Everything that goes to the ultimate consumer.

Mr. **Patman** (reading):

> to ultimate consumers who are natural persons, for their individual or family use and not for resale.

Mr. **Goldsborough**. That is right.

Mr. **Patman**. In other words, those are the necessities of life?

Mr. **Goldsborough**. They are necessities, and I hope that they are luxuries.

Mr. **Patman**. That is right, and the comforts of life, and you think that by reason of that 15-percent discount it will increase the demand that much?

Mr. **Goldsborough**. Yes.

Mr. **Patman**. Increase the demand that will cause the factories to increase their output 15 percent?

Mr. **Goldsborough**. Correct.

Mr. **Patman**. By restricting it to the ultimate consumers, to natural persons, you greatly restrict the distribution.

Now, I presume that under this a man would be allowed to buy one automobile, but if he needed two for his own use, would he get the 15-percent discount?

Mr. **Goldsborough**. Yes.

Mr. **Patman**. If you had an automobile to sell, and it was a certain well-known model, we will say a 1937 Ford, and it had only been run 500 miles, and I was a dealer and I had a Ford just exactly the same, in the same condition and everything, and you wanted $700 for your car, and the chairman of the committee wanted to buy it, he could not afford to buy it from you; he would have to buy it from me, because I am a dealer, and I have a license from the Secretary of the Treasury, and I could give him a 15-percent discount, but you could not give that to him, could you?

Mr. **Goldsborough**. No.

Mr. **Patman**. What about the man that wanted a yacht?

Mr. **Goldsborough**. May I supplement my answer?

Mr. **Patman**. Yes, sir.

Mr. **Goldsborough**. By saying that the individual who buys a second-hand car would get a much better price for his car, by reason of the fact that the dealer would be able to buy his car for 15 percent more than he otherwise could, because he in turn could give a prospective purchaser a 15-percent discount.

Mr. **Patman**. But that would force the business to go through the licensed dealers of the country?

Mr. **Goldsborough**. There is no question about that.

Mr. **Patman**. And the licenses would get to be quite valuable in a case like that.

Would a license to do business be unrestricted? Would they have a certain number, or any number?

Mr. **Goldsborough**. Mr. Patman, as to whether this discount will be 15 percent or more, in my opinion it would probably be more, because I think that we are able to produce twice as much as we are producing now of goods and services, so that the discount would probably be much greater than 15 percent, but whether or not more people would get in the retail business than are now in it, I cannot answer that.

Mr. **Patman**. I understand from reading your bill and from your explanation of it that the Secretary of the Treasury, or this Board that is to be set up under your bill, will require a certain voucher to be made out on each sale. Is that right?

Mr. **Goldsborough**. I would think that the mechanics of it, that the regulations, would have to require something of that kind. There is nothing about that in the bill. That would have to be under the regulations. There would have to be something to prevent fraud on the part of the retailer.

Mr. **Patman**. It would require some bookkeeping, some supervision, some investigation and report if, for instance, you went to the corner drug store and made a 50-cent purchase, for in order to get the benefit of that 15-percent discount, you would have to sign the vouchers and make the proper certificate to show that you are a natural person, and an ultimate consumer, and that therefore you are entitled to the 15 percent?

Mr. **Goldsborough**. Just what the ultimate regulation would be I cannot visualize, but I have thought of that feature in connection with the operation of a sales tax. In New York City, for instance, if you buy anything at retail in a drug store or anywhere else, there is a certain tax that you have to pay. It is sometimes 1 cent, sometimes 2 cents, sometimes 25 cents, but everybody who purchases goods in New York has to pay that tax, and it appears to be operating easily, successfully, and efficiently, and I do not see that the operation of this bill would be any more difficult than the operation of a sales tax.

Mr. **Patman**. But, anyhow, in order to look after it——

Mr. **Goldsborough**. Just what the method would ultimately be I do not know.

Mr. **Patman**. These sales have to be made only to ultimate consumers, to natural persons?

Mr. **Goldsborough**. That is correct.

Mr. **Patman**. And they must be made for that particular consumer, and not for the purposes of resale?

Mr. **Goldsborough**. That is right.

Mr. **Patman**. Some evidence of that must be certified to, or the Government would be running quite a risk of not getting these payments. So I think that the logical course would be to have a statement for each customer to sign on every purchase, and on that statement he would have to certify that he was a natural person, that he was an ultimate consumer, that it was not for resale, and the man making the sale would have to acknowledge that, or O. K. it, and then he would have to take it back to his books and make the proper record, and then at the proper time he would take all of those slips covering a 15-cent package of cigarettes, of a $1 article, or even an automobile, and he would take them to the bank and would say to the banker, "I am entitled to the 15-percent discount on these." Assuming that they all aggregated $100, not counting the discount, that is when the bank would give that man credit for $100 on the books, and that is when the Government would issue to that bank $100 of its interbank currency, would it not?

Mr. **Goldsborough**. I do not visualize all of that complicated machinery that you have in mind. I think that human ingenuity is such that it would be very easy to devise a much simpler system than what you have in mind.

Mr. **Patman**. Without opening it up to the possibility of fraud?

Mr. GOLDSBOROUGH. Yes. You take my town, for instance. The bankers know the citizens of that town. They would catch a fraud in a very few minutes. Just how it would operate in a large city I have not worked that out in my mind, but as I indicated awhile ago, it seems to me that it would be just as easy to operate a system of this kind as it is operated under the sales tax.

Mr. PATMAN. They would have no incentive to catch the fraud. Why should the merchant try to detect it? He is not going to make enemies.

Mr. GOLDSBOROUGH. You cannot be guilty of fraud without its getting broadcasted, you know. Just as the Government has to have investigators to go around from time to time, to see if the Government tax is properly paid, you probably would have to have a Government inspector to go around from time to time to see if there is any fraud going on.

Mr. PATMAN. Who would have the incentive to disclose that fraud? You see, the merchant who has made the sale has no incentive to try to detect fraud. All that he wants is the proper voucher filled out, so that he can carry it to the bank, and then when the voucher is signed there is no incentive for the local banker to detect any fraud. Why should be make enemies by snooping around to try to find out if anybody has violated the law, when he will get his money? So there is no incentive to prevent fraud.

Mr. GOLDSBOROUGH. You probably have not considered the fact, which is perfectly apparent to me, that the competition among the retailers would naturally be such that they would not permit fraud.

Mr. PATMAN. Would not permit it?

Mr. GOLDSBOROUGH. You cannot conceive of a half dozen retailers getting their heads together in order to beat this discount—at least, I cannot.

Mr. PATMAN. I know, Mr. Goldsborough——

Mr. GOLDSBOROUGH (interposing). And, unless they did get their heads together, it would not work.

Mr. PATMAN. But suppose now that I had an automobile myself, and I should want to buy another one, so I went to some merchant in a nearby town and got the automobile sold to me for a 15-percent discount; what is to keep me then from turning around and selling it to somebody else, and making a little money on that?

Mr. GOLDSBOROUGH. Mr. Patman, of course I do not think that anyone could possibly answer categorically the questions which appear to be of interest to you, any more than he could anticipate the evasions of the income tax which we are now reading about every day in the newspapers. It is perfectly evident that people will try to avoid this law, just as they are trying to avoid taxes and other laws. I have no doubt that there would be difficulties, but to my mind the difficulties are the simple and normal ones of carrying out any piece of legislation, and I do not conceive at all the complications which apparently are disturbing you.

Mr. PATMAN. You do not think that there would be any danger of any fraud of that kind?

Mr. GOLDSBOROUGH. I do not say that. I think there would, just as there is a danger of fraud in any other human transaction, but I do not see that the dangers brought about by the operation of this law would be any greater than the dangers brought about in the operation of any law where human interest is involved.

Mr. **Patman.** Of course, in this situation there are over a million and a half retailers involved, and over 100,000,000 people, and naturally there would be more opportunities for fraud, since this deals with every comfort, convenience, and luxury in life.

Mr. **Ford.** May I ask one question there?

Mr. **Patman.** Let me pursue this one question further, and I will be through. When this merchant has accumulated all these vouchers properly certified to that will entitle him to this 15-percent discount, and he takes them to the bank, this bill says that the banker has a right to levy a reasonable service charge against him for giving him that 15 percent.

Mr. **Goldsborough.** No; the service charge would be fixed by the Federal Credit Commission.

Mr. **Patman.** And it would be taken out of the 15 percent?

Mr. **Goldsborough.** That is correct.

Mr. **Patman.** All right. Then the customer evidently will not get the 15 percent, because the merchant will make him pay that.

Mr. **Goldsborough.** If it is necessary in order to distribute the goods and services which can be produced to increase that 15 to 17 percent, it would be done.

Mr. **Patman.** It would be done by the commission. Now, this local merchant takes $100 of these vouchers properly signed to this local bank, and the bank gives him credit for $100, and the bank would be entitled to $100 of interbank currency. Where does that actually come from, this $100 of interbank currency?

Mr. **Goldsborough.** From the Federal Credit Commission.

Mr. **Patman.** The bank would send these vouchers to the Federal Credit Commission?

Mr. **Goldsborough.** What the bank actually would get in practice, Mr. Patman, would be just what a bank gets now at the Federal Reserve bank.

Mr. **Patman.** But suppose that the bank said, "I want something tangible."

Mr. **Goldsborough.** It would get the credit, in practice, but if it wanted the interbank currency, it would get that.

Mr. **Patman.** What would be on this currency, the wording of it?

Mr. **Goldsborough.** I presume, of course, and it is a perfectly natural and normal presumption, that there would be the proper wording on it to indicate that it was interbank currency issued by the Federal Credit Commission to carry out the provisions of this law.

Mr. **Patman.** Secured by what?

Mr. **Goldsborough.** Secured by the goods which it creates by its operation.

Mr. **Patman.** But, as I understand it, those goods have already gone to the consumer.

Mr. **Goldsborough.** They do not get to the consumer except by the operation of this law.

Mr. **Patman.** Now, then, would that be an obligation of the United States Government? Would that say, "The United States Government promises to pay the borrower $100"?

Mr. Goldsborough. No; this currency could only be used by the banks in normal conditions for two purposes, to settle balances with other banks and be used as a 100-percent backing for its deposits.

Mr. Patman. I know, but this banker receives this interbank currency, this $100, and he says, "I do not want this; I want money." Where would he carry that to get the money?

Mr. Goldsborough. He could not get anything except the interbank currency.

Mr. Patman. I know, but he says, "I do not want this; I want money; I have got to have money; I have to pay my own bills."

Mr. Goldsborough. I do not know what your question is. Nobody could answer that question, Mr. Patman, because he does not get this interbank currency which he in turn can use——

Mr. Patman (interposing). But suppose that he gets so much of it that he wants some money to take care of his cash transactions?

Mr. Goldsborough. This does not interfere in any way with the normal operations of his bank. It does not lessen in any sense his ordinary deposits. It does not interfere in any way with his ordinary transactions. The purpose of this bill, the deliberate purpose of it, is to create a new agency which in no way interferes with the normal operations of a bank. This particular account would be separate and distinct from any other operation that a bank has, and the only difference between the money created by this discount and the money created by law would be that in the one case the loan is secured by the collateral that the borrower puts up, and in the other case it is secured by the goods which are created by virtue of the operation of the law.

Mr. Patman. But, Mr. Goldsborough, we cannot keep it in circulation. That is money of the banks. It has been issued. It is the obligation of somebody, and somebody must redeem it at some time under some conditions, and who will redeem it, and how?

Mr. Goldsborough. The only answer that I can make is that I do not understand your question, because I do not think that it has any relation to the bill.

Mr. Patman. All right. Now, suppose that this man has $100 and it is in bank currency, and he has to get the money somewhere. He cannot get any money on this interbank currency, and therefore he has a frozen asset.

Mr. Goldsborough. Oh, no.

Mr. Patman. How can he use it?

Mr. Goldsborough. He can use it as 100-percent backing.

Mr. Patman. To borrow money?

Mr. Goldsborough. To loan money to his customers.

Mr. Patman. To loan money?

Mr. Goldsborough. To loan money to his customers.

Mr. Patman. But he does not want to loan it; he wants the money himself.

Mr. Goldsborough. He has the money that he gets from the ordinary operations of the bank. This does not interfere at all with the present profits that he makes in the ordinary operations of the bank. It is an entirely separate department of the Government, and has no relation whatever to the ordinary operations of the bank, and it does not interfere with them.

Mr. Patman. Do you propose under this to put silver or gold behind it, or either or neither?

Mr. Goldsborough. No; of course not.

Mr. Patman. What will be behind this money that is issued? Suppose that there is five billion of it issued; what will be the security, and who will redeem it?

Mr. Goldsborough. It will be secured by the goods which it creates, and it therefore cannot be inflationary.

Mr. Patman. Now, suppose——

Mr. Goldsborough (interposing). I will try to illustrate so that you can get the picture that is evidenced by the bill. If you have 50 bushels of wheat and $50 in circulation, you have a bushel of wheat balanced by a dollar. Now, if you increase your production of wheat to 100 bushels, you can put out $50 more, and you still have your dollars balanced by bushels of wheat, so that you are not going to have an inflation; and when this discount is allowed, and production and distribution are increased to the extent of the discount, you have this money balanced by the goods which are produced by virtue of the discount.

Mr. Ford. Could I make a statement?

Mr. Patman. One more question and I will be through, I assure you. Is there anything in this bill that will prohibit the retailers from increasing their prices 15 percent and then collecting that 15 percent through the banks?

Mr. Goldsborough. Mr. Patman, it is perfectly evident that competition would take care of that situation exactly as it takes care of similar situations now. There would be absolutely no difference insofar as the temptation to increase prices is concerned with this bill in operation than the temptation which arises now, because the bill would operate among the retailers who had licenses.

Mr. Patman. Mr. Goldsborough, I have studied this with more than passing interest because you were the author of it——

Mr. Goldsborough (interposing). I have tried to answer your questions.

Mr. Patman. I have really studied it, and I studied your speech the other day, and I wish that I could see it like you do, but I do not. I know that your object is to get money out among the masses, and that is a commendable purpose; but I just cannot see where this is the right vehicle to use. But I am going to keep on studying it, and if I can see your viewpoint I am sure that I will be very glad to support it.

Mr. Goldsborough. The purpose of these hearings, of course, is to get all the light that can possibly be thrown upon this subject; and I am very certain that the committee, the House and Congress, as well as the country, will be very much interested in the observations that you made this morning; and I understand fully that all that you are trying to do, and all that I am trying to do, is to find the solution to the problem that exists.

Mr. Patman. Surely. I enjoy studying any plan, and I enjoyed studying this plan, and I shall continue to study it sympathetically; but I just cannot see but what the troubles and obstacles that you will be confronted with will overbalance the good and open the floodgates to all kinds of fraud against the Government, so that nobody will be able to properly protect and safeguard the public interest.

Mr. Ford. Let me ask you this question: Does not this plan that you have bring into being this bank currency only when a situation exists where business begins to lag, when invoices begin to decrease, and distribution slows up? Isn't that its purpose?

Mr. Goldsborough. That is, in my opinion, a full statement of its purpose.

Mr. Ford. That approximates your plan?

Mr. Goldsborough. That, of course, would cover the point of view of the businessman and, to a certain extent, the point of view of the banker; but it seems to me that a complete statement of the purpose would be an effort to cure the situation which we have in this country and in other civilized countries of poverty in the midst of plenty. To solve the problem of being able to distribute to our people all that our people are able to produce, as I conceive it, is a broad statement of the purposes of the legislation.

Mr. Ford. All right. Now, at the present moment there is no question in my mind and in the minds of people who have made a study of it that we are capable in the United States today of producing considerably more of the products than the people are able to purchase. That is so, is it not?

Mr. Goldsborough. Yes.

Mr. Ford. Your plan then is, in view of that, to encourage manufacturers, miners, lumbermen, general producers, farmers, and all the rest of them to go ahead and produce to capacity?

Mr. Goldsborough. Yes.

Mr. Ford. When that capacity production comes on the market to be distributed, we find that there is not sufficient purchasing money in the country to absorb it, and that in order to permit the manufacturer to go safely ahead and produce it, the Government will step in, through this interbank currency, and put up as much as 15 percent of the lag?

Mr. Goldsborough. That is the initial provision in the bill, Mr. Ford; but the Federal Credit Commission would be bound to carry the investigations continuously, so that this discount would be changed from time to time.

Mr. Ford. We will say that they have made an investigation and they find that only 10 percent is necessary to take up the lag, and then they go to the bank. Your customers are doing business, and there are a million or two, and after they have sold the goods at the price that they can get on this market, which is presumably the amount that the consumer can afford to pay, there is a discrepancy of 10 percent in the man's total monthly business, so that he goes to the bank and he says, "I have sold everything that I had, but in order to sell it I had to cut the price, and I cut it 10 percent. Instead of depositing $100,000 with you, I will only deposit with you $90,000, but you should give me credit on your books for $100,000." That is the way it works?

Mr. Goldsborough. Yes.

Mr. Ford. And the bank says, "We will give you credit for $100,000, although you actually put in $90,000."

Then the bank certifies it to the Secretary of the Treasury, and in the meanwhile the Federal Credit Board has made its investigation and has found that 10 percent is the actual amount of the lag, and the

Treasury certifies back to the bank that they will make that deficiency good. That is the situation that you are contemplating?

Mr. **Goldsborough.** That is correct.

Mr. **Ford.** Then I think I understand what you are trying to do.

Mr. **Goldsborough.** And then, as to that 10 percent, Mr. Ford, the bank would have the right to make a bookkeeping entry there on which they could loan.

Mr. **Hancock.** Just one more question, Mr. Chairman, supplementing one of the questions propounded by Mr. Patman.

What would happen to this interbank currency in the event the bank liquidated?

Mr. **Goldsborough.** In event the bank failed?

Mr. **Hancock.** Yes. Would it constitute an asset of the bank; and if so, how would the individual stockholders or depositors participate in it?

Mr. **Goldsborough.** Well, I have not given that consideration, to what would happen if the bank liquidated, but if this bill——

Mr. **Hancock** (interposing). Suppose——

Mr. **Goldsborough** (interposing). Let me finish. When this bill is taken up and is read for amendments, I presume that a provision would be made which would render that interbank currency available as an asset. There is a provision in the bill which states that this interbank currency, if a bank gets into difficulties, can be exchanged for real money for the purpose of supporting the bank, and after the bank gets back on its feet it would have to take interbank currency again and deliver up the cash that it received from the Secretary of the Treasury.

Mr. **Hancock.** Suppose that a licensed retailer desired to liquidate his business, and had several hundred thousand dollars in discounts?

Mr. **Goldsborough.** It does not affect the retailer at all. The money that he puts in the bank, which represents this discount, is just like any other money so far as he is concerned.

Mr. **Hancock.** He could take it and draw out of the bank other currency in lieu of the interbank currency?

Mr. **Goldsborough.** Oh, yes; he would not get the interbank currency. The money that the retailer gets is just like any other. The bank has to give him credit for that deposit just like any other deposit. He is not affected one way or the other under this bill.

Mr. **Farley.** Mr. Goldsborough, what would be the effect upon this legislation if all business in the country decided suddenly to go on a cash basis, cash and carry?

Mr. **Goldsborough.** Of course, I want to answer your question, and I would be very happy myself if we could get out of the installment business, and in my judgment, the operation of this law would gradually assist us in getting out of doing business on the installment basis. The reason that they do business on the installment basis is because of the shortage of money. If we had a proper circulating medium, it would not be necessary to sell goods at retail on the installment basis, and the result of selling goods on the installment basis is inevitably a choking up of credit, resulting in these collapses and depressions. There cannot be any other ultimate result. This system that we have of selling on the installment basis simply means that we have, from time to time, to burst.

Mr. **Farley**. We have too much credit then, right now?

Mr. **Goldsborough**. Yes.

Mr. **Ford**. There is $14,000,000,000 of it right now, on the installment plan.

Mr. **Goldsborough**. Yes; and the installment-plan credit inevitably accumulates and gets larger and larger, until it becomes so top-heavy that business collapses; it just has to do it.

Mr. **Hancock**. If this bill would aid in relieving the people of debt and ultimately enable everybody in the country to get out of debt, we would still be, according to your contention, without any medium of exchange, would we not?

Mr. **Goldsborough**. I do not think so, sir.

Mr. Chairman, I have the first bill in the omnibus claims bill that is coming up, and I really have to get to the floor.

Mr. **Hancock**. We can carry that question over to another time.

Mr. **Patman**. Would you try to obtain some information between now and the next hearing as to the number of people that might be required in the way of retailers' extra help to carry out these transactions to make out these vouchers, and also that same information with respect to the banks, and the probable extra expense?

Mr. **Goldsborough**. I am afraid that you will have to conduct your investigation yourself.

Mr. **Patman**. And also the number of transactions that would be involved?

Mr. **Goldsborough**. Mr. Patman, the question is not a serious question at all to me.

Mr. **Patman**. I see.

Mr. **Goldsborough**. If you deem it so, you make your own investigation.

I think that that is a fair answer.

Mr. **Crawford**. I have several questions that I wanted to ask Mr. Goldsborough, but he has just stated that he wants to go on the floor, so these questions can go over.

Mr. **Goldsborough**. Mr. Chairman, Mr. Harvey is here this morning. Of course, he cannot be heard this morning, but Mr. Harr, commissioner of banking of Pennsylvania, and Mr. Benjamin Anderson, a professor of political economy at New York University, also want to be heard; and I would like to be informed when these hearings are likely to be resumed. From what you said this morning I presume that you have other matters that you want to take up this week.

(Thereupon there was an informal discussion off the record, following which it was decided that the committee would meet at 10:30 the following morning, Wednesday, July 14, to consider other matters, and the date of a further hearing on this bill was left undetermined.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

TUESDAY, JULY 20, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., to resume consideration of H. R. 7188, Hon. Henry B. Steagall (chairman) presiding. Other members present: Messrs. Goldsborough, Williams, Spence, Meeks, Ford, Brown, Patman, McKeough, Transue, Wolcott, Luce, Crawford.

The **Chairman**. The committee will come to order. Mr. Goldsborough is recognized for the continuance of his statement. I understand that Mr. Crawford would like to interrogate him.

Mr. **Crawford**. Mr. Goldsborough——

The **Chairman**. Have you any further statement that you wish to make?

Mr. **Goldsborough**. No further statement.

The **Chairman**. Mr. Crawford, you are recognized.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. **Crawford**. Mr. Goldsborough, if I understood you correctly when you made your opening statement, your contention is to the effect that the only remaining obstacle to full speed ahead in industrial activity and a constant high level of individual possession depends upon the best selection for putting the money rules into operation.

Mr. **Goldsborough**. Is that a question, or just a preliminary statement?

Mr. **Crawford**. Yes, sir; that is a question.

Mr. **Goldsborough**. Mr. Crawford, I do not want to make any arbitrary statement, because I do not think that I am wise enough to be able to formulate a legislative measure which will assure the cure of our economic ills. What I am trying to do is this: To find a correct relationship between industry and the monetary system, and if we can find that, I think that it will so clarify the business atmosphere that our other difficulties, such as our unemployment, being unable to balance the Budget, and taxes so onerous as to constitute a general complaint, can be taken care of. That is my feeling, and as far as I know myself, this bill in its operation undertakes to find, and I believe does find, the correct relationship between the monetary system and industry.

Now, I do not know whether that is a satisfactory answer on that or not. I want to answer your question, if I can.

Mr. CRAWFORD. You feel, then, that there is a very definite relation between the flow of goods and the flow of dollars?

Mr. GOLDSBOROUGH. Yes; I do, positively. I will state it in another way. I believe that in a simple civilization, where the things that we want and need are made with the hands, the law of supply and demand as between money and the things that money can distribute, was definite and actually existed, and what I am trying to do is to reestablish the law of supply and demand in a power economy, as between the things people want and the medium of exchange which they use to get the things that they want. I think that the law of supply and demand has been lost in the power economy as between money and the things that money can distribute.

Mr. CRAWFORD. That really directly relates to my question, because when Governor Eccles was before the committee some time ago I raised with him the question of the willingness of the businessman or the enterpriser to get along with the banks, that the banks could not same loans until someone was willing to come along and assume the risk of seeing that that loan was made to the borrower.

Now, if there is in your bill a mechanism which creates an economic condition between the fellow who desires to adventure in business and thus employ people and thus create goods and the fellow who has credits to extend, meaning the banker, of course, I am very anxious to have you bring out in the most direct manner possible, just where that mechanism is and how it would work, and also whether or not it will work in a manner which will meet the changing psychology of the individual and the moods and impulses of the people when fear begins to grip and when loans begin to be called or credit contracted, to the end that employment and production will start to pick up at a point where the depression begins to step in.

Mr. GOLDSBOROUGH. Let us assume that a depression is beginning, the indications being that the bankers are beginning to call in loans, prices are falling, and unemployment starts. Now, the establishment of this discount rate or its increase at a time of that kind would, in my opinion, undoubtedly reestablish buying power in the masses of the people, and that discount could be increased indefinitely until it did reestablish the buying power of the masses of the people. As soon as that buying power was reestablished your difficulties would be over automatically; all of your economic difficulties would be over as soon as the buying power of the masses of the people is reestablished, because that affects not only the retail trade, the wholesale trade, the manufacturer, and the prime producer, but it also immediately reestablishes the currency on a sound basis, because the banks, as soon as production is established, cease to have any fear and they cease to call in their loans.

Mr. CRAWFORD. Have you that knowledge of the mechanism that you refer to well enough in hand so as to make a statement to us that you feel that the increasing of the discount will impel action on the part of the people and enterprises to employ workers and produce goods, and will it also furnish the foundation for those goods to move at profitable prices, thereby bringing about profit, which, after all, is the incentive for going into business?

Mr. GOLDSBOROUGH. The picture that I see would be this: That the individual whose income has been depleted because of an incipient depression will have his buying power reestablished by the discount, and when his buying power is reestablished he can buy as much as he did before and automatically the business of the retailers and of the producers is reestablished, the confidence of the banker is restored, and the country is again on a normal business basis. That is the picture that I see.

Of course, my deductions may be wrong, but I do not think so, and while I do not believe in the inductive process particularly, it is interesting that I have received several letters in the last few days from people whom I thought would be very antagonistic to this thing. They are private for the time being, but these people will appear before the committee later if the hearings continue.

The only criticism that I have received is the fear that if the buyer, the ultimate consumer, knows about this discount he will not understand the reason for it, and that, therefore, he will complain if it is reduced or abolished altogether, as the case might be. In other words, I have had no criticism except on the mechanism of the bill; no criticism of the principle involved. I personally think that that difficulty can be cured by an amendment, so that as far as the consumer is concerned he will not know about the discount any more than he knows that because of the tariff or what not he has to pay more than he otherwise would pay. I do not see why it cannot be done.

Mr. **Crawford.** You say that you think this bill should be amended so that the consumer would not be cognizant of the amount of the discount?

Mr. **Goldsborough.** Of the discount at all. All that he would know is that he is buying whatever he buys cheaper. For instance, a Government inspector, a city inspector, or a county inspector, as the case may be, goes around from time to time where there is a sales tax, and he looks through the books of the retailer or he looks through the books of the moving-picture owner, and he is able pretty well to tell whether he is getting correct information. Of course, there is some fraud; there is bound to be; but I personally do not believe that it is impossible at all, after a little experimental regulation, for the Government agents, that is, the agents for the Federal Credit Commission that is set up in this bill, and the retailer, to establish such a relationship that the Federal Credit Commission inspector can tell pretty well whether he is getting a square deal from the retailer without any receipt at all from the consumer.

The difficulty that I have seen about this bill from its inception has been that difficulty, and that is the only difficulty that I have ever seen in it, the fact that the consumer, if he is in the habit of getting a discount, and that discount was reduced, would immediately think that somebody was chiseling him or that somebody was cheating him, and so far as undertaking to explain to the consumer the mechanism of legislation of this kind, it is simply out of the question.

Mr. **Crawford.** If you should make that amendment, it would get away from that question which was raised by Mr. Patman the other day with reference to the consumer signing a voucher, and the bookkeeping routine that would be incident thereto.

Mr. **Goldsborough.** You could get rid of it, and also get rid of the psychology that we have been discussing this morning.

Mr. **Crawford.** As I comprehend the operation of the Federal Reserve Banking System and its importance so far as the granting of credit is concerned, it moves in the direction of extending credit to a community as it wishes to use more credit, which is indicated by the member bank making an application to the Federal Reserve System. Is that your comprehension of it?

Mr. **Goldsborough**. That is correct, I am sure.

Mr. **Crawford**. May I ask you if you feel that your bill in its present form, with some amendments thereto, would still leave the dollar flow or the granting of credit, the issuance of dollars to individual initiative, as indicated by the application of the banker to the Federal Reserve System, or would it bring about the assumption of issuing credit by the Government, making it a national responsibility to impel its operation? Do you feel that there is that strength and impelling force in your retail discount?

Mr. **Goldsborough**. I am not just entirely sure that I understand your question fully.

Mr. **Crawford**. Let me say it in this way, because I do not believe that that is clear.

Suppose that economic fear is beginning to grip the country. I go to the bank and I say, "Mr. Member Banker, I desire to make a loan of $10,000 to help in the actual production and distribution of goods." The banker says, "I will tell you; I do not think that we want to make any more loans."

Mr. **Goldsborough**. Why would he say that?

Mr. **Crawford**. Because of fear. It is this mood that the banks of the country will be getting into, we will say, by reason of some kind of an economic situation which they think is coming. It might be caused by international or by political conditions.

Mr. **Goldsborough**. I wonder if I can interject there advantageously. Let us suppose that this discount began to operate, and the banker woke up next morning and found that there was business going on downtown, and that production was being resumed. Would not that dispel his fear, and would he not then feel like lending the $10,000?

Mr. **Crawford**. It might, if his fear had been caused by local conditions in the first place, but——

Mr. **Goldsborough**. Well, this discount would operate all through the country. It would not only correct a local condition, but would correct a general condition.

Mr. **Crawford**. It seems to me that the one great weakness of the Federal Reserve System is that we have not put an impelling force in there, so that when the banking industry begins to contract credit and to destroy currency, if you please, the Federal Reserve responsibility does not offset that and force the situation back in the other direction leading to a call on people for the production of goods, and thereby counteracting the bad influence which is caused by the contracting of credit by the banker, because of fear, or mood, or psychology, or whatever you might call it.

Mr. **Goldsborough**. You see, Mr. Crawford, the reason for that is this: that the Federal Reserve System is not an original conception in this country at all. It is built up from the central bank system in Europe, and instead of being primarily created for social purposes, it was primarily created for the purposes of the bankers. That is one difficulty about the Federal Reserve System. Now, that has been helped, but it is still hampered by reason of the fact that it is a creature of a banking system rather than of a social system.

Mr. **Crawford**. Right in that connection, do you believe that the Federal Reserve System, after these recent acts, is now empowered to initiate the flow of dollars?

Mr. **Goldsborough**. It cannot do that, because the only thing that it can do along that line is to make credit.

Now——

Mr. **Crawford**. Do you mean by that, upon the application of the member bank?

Mr. **Goldsborough**. That is correct. That is the only thing it can do.

Now, I want to illustrate that by using an illustration that I used in the hearings of 1935. You can pull a string, but you cannot push a string, and when the country is in the grip of fear, you can have all the credit in the world but it won't be utilized. That is when you try to push a string. If you put buying power by means of this discount or some other legitimate means into the hands of the ultimate consumer, you are pulling a string then. You are not pushing it.

Mr. **Crawford**. In other words, you are trying to work into your bill a mechanism which will correct the trouble that faces us at the moment, to get our present banking laws and procedure so that your mechanism will actually create a demand for goods, and that that demand will be covered by this interbank currency, based on the retail discount?

Mr. **Goldsborough**. Yes.

Mr. **Crawford**. Then you feel that at the present time the Federal Reserve System does not so function as to actually create a demand for credit?

Mr. **Goldsborough**. It cannot do it. Of course, in the long run, Mr. Crawford, it will have, I am sure, an effect, but for years now it has been so impossible to use the available credit that interest rates have gone down to almost nothing, and Mr. Eccles, who testified here the other day on another bill, stated that one of the reasons for raising the requirements was to assist in an increase in the interest rates. Of course, when that condition exists, as long as that mental operation of the country is such that they are not using the available credit, it is serving no purpose whatever, but I have no doubt that ultimately it does have a psychological effect.

But let us assume now that in the latter part of 1929 there had been in operation something like the plan proposed in this bill which could have been utilized. All of these alphabetical organizations would have been absolutely unnecessary, because you could have reestablished buying power in the masses of the people, and that would have reestablished the ordinary run of business.

Mr. **Crawford**. Would you add to that that the stimulation of industrial activity by increasing the Federal debt and selling bonds would also have been unnecessary?

Mr. **Goldsborough**. Absolutely, entirely so; because the increase of the Federal debt has been utilized for the purpose of carrying on these alphabetical organizations.

Mr. **Crawford**. Then, I assume, by reason of the fact that you have introduced your bill, that you do not believe that the responsibility of Congress has been or will have been discharged until we do something along the lines that your bill favors, or make such changes in the Federal Reserve set-up as will enable the Federal Reserve System to initiate a demand for credit?

Mr. **Goldsborough.** I say the Federal Reserve System or some other Federal agency.

Mr. **Crawford.** Yes; in connection with the banking and the monetary policy of the country.

Mr. **Goldsborough.** Yes.

Mr. **Crawford.** What do you think about this: That if Congress fails to take the action that you have just mentioned, does it not, in fact, contribute to a confiscation of the people's property without due process of law, and in contradiction to the guarantys in the Constitution, in that through a lack or absence of a properly operating banking and credit system, we permit these depressions and financial wash-outs, thereby destroying the equities of the people, such as occurred in 1929 and 1933?

Would you go so far as to say that?

Mr. **Goldsborough.** I will just go so far as to say that in my opinion legislation can be passed which will make it impossible for the wealth of any individual or set of individuals, which has been accumulated by legitimate means, from being simply wiped off the earth, and I would go so far as to say that now that the banking system, because of this depresison, is cognizant of its weakness, that the banking system itself should be the first to cooperate with other social forces to make it impossible for that condition ever to happen again.

Mr. **Crawford.** That directly answers my question, and that is the thought that I wanted to bring out.

Now, if this retail discount and the interbank currency are created, do you feel that the mechanism that you have put into your bill will permit any of this newly created currency to be used for speculative purposes, or will its operation be restricted entirely to the production and distribution of goods on a profitable basis?

Mr. **Goldsborough.** It cannot be used for any other purpose except production, for this reason, that currency does not come into being until the goods which are created by virtue of the discount go to the ultimate consumer. It has no relation whatever to speculation, and it has no relation whatsoever to long-term credit; it is only used for the purpose of getting goods to the ultimate consumer. It has no relationship whatever to the speculative process.

Mr. **Crawford.** If I understand your bill correctly, and your explanation, it would appear that this interbank currency which is in a way credited on the passbook of the retailer if he makes his deposit of credit amounting to a retail discount, will, in a way, take the place of a loan to the retailer.

Mr. **Goldsborough.** Yes; that is true.

Mr. **Crawford.** Now, do you feel——

Mr. **Goldsborough.** A loan which he does not have to repay.

Mr. **Crawford.** Do you feel that the interjection of that mechanism into our banking system will to a large degree displace the loans now made by the banks, according to the old, customary procedure?

Mr. **Goldsborough.** Well, if it does, it will be a good many years before that takes place. Its first effect, and its effect for many years to come, would be to enable the banks to continue the process of commercial loans without any possible danger of the bottom dropping out of the value of the collateral, because as soon as a depression started, this retail discount would immediately come into operation, which would reestablish production and distribution, and which therefore would keep up the selling price of the securities which the banks hold as collateral for their loans, so that insofar as the banks are concerned, the operation of this law would be absolutely beneficial.

Mr. **Crawford**. And at the same time the amount of interbank currency would expand or contract, absolutely independently of the policies of the private bankers?

Mr. **Goldsborough**. Absolutely. The intent was to so frame this bill that it would not interfere in any way whatever with normal banking operations, but insofar as the banks are concerned, it would serve the purpose of preventing the values of the securities held by them as collateral for their loans being lowered, and it would constantly reestablish the value of the securities held by the banks by reestablishing the buying power of the masses of the people. It would automatically do it.

There is not anything in this bill, and it was deliberately framed with an attempt not to interfere at all with the normal operation of the banking business, but simply to assist the banking system in carrying along on an even keel. One of the things that I recognized, and I have recognized it for many years but have not been able to avoid it and I have not found any means of avoiding it unless it is avoided by this bill, is the tremendous opposition of the banking system to any monetary measure which they think would interfere with their processes. Now, this does not interfere with their processes. It prevents the collapse of their processes.

Mr. **Crawford**. Then, in that connection, you feel that this bill would tend to synchronize the total flow of all goods to the total flow of all money?

Mr. **Goldsborough**. Yes.

Mr. **Crawford**. And not just that proportion which is represented by the retail discount?

Mr. **Goldsborough**. Absolutely.

Mr. **Crawford**. That is all that I have.

The **Chairman**. Gentlemen, are there any further questions of Mr. Goldsborough?

Mr. **Ford**. May I ask Mr. Goldsborough a question?

Mr. Goldsborough, I have read your bill very carefully, and, as I told you before, there are one or two things in it that just do not seem to register. But this question is aside from your bill. Do you think that it would be a good thing to apply the F. H. A. principle to insuring commercial loans—and I realize that you are opposed to credit——

Mr. **Goldsborough**. I do not mean to contradict you, sir, but if you ever understood me as saying that I was opposed to credit, you have misunderstood me.

Mr. **Ford**. I am sorry that I did.

Mr. **Goldsborough**. I think that credit is necessary.

Mr. **Ford**. I understood you to say on the floor that our money was all based on credit, and by reason of that fact it was unsound money.

Mr. **Goldsborough**. What I intended to convey was this: That it was, in my opinion, unsound to have a monetary system where business could not be done on any other basis except debt, and where it was impossible to pay a debt, impossible for society to pay its debt under the present monetary system, I stated that I thought we ought to have a system where debt would be an incident rather than a necessary complement to practically every business transaction, and I think that that is sound.

Mr. **Ford**. There are facets of that jewel which I agree with, but I just want to ask this question, because I know that you have given the subject of banking and credit a good deal of thought. We applied the principle of insuring loans to the F. H. A., and the result of that has been to bring out private money to the extent of billions into circulation in order to put it into homes. I am wondering if we could not apply that same principle to insuring commercial loans, and that if we did it would not permit literally hundreds of thousands of small business institutions to get loans that the banks otherwise would not make. If it only had the result of increasing the commercial loans of the country 20 percent, would that not put a lot of money into circulation, which, in turn, would employ a lot of labor and would enable a lot of small plants which are at the present time inadequately financed to go ahead with their operations and produce goods at a price so that those goods could be marketed, and that, in turn, would put a lot of men to work?

Do you not think that that is so?

Mr. **Goldsborough**. Mr. Ford, I wish that I could give you my opinion on that, but I cannot because I have not thought about it. It is a novel suggestion to me, and I have not given it proper consideration, and for that reason I do not think I am able at the moment to give you my opinion. But the thing that flashes immediately across my mind is this: Whether or not a system of insuring commercial loans would not tend very strongly to create unsound credit practices. That is the thing that flashes across my mind right off the bat, but——

Mr. **Ford**. The present situation is such that we get complaints from all over the country that small business is unable to get loans from banks. I will talk to the bankers about it, and they say, "We would like to lend those fellows money, but we are lending your money and the other fellow's money, and we have got to be careful, and they think that they ought to get $20,000, when we think that they should have $5,000," but if that fellow took that $5,000 he would merely get in debt, whereas if he had the $20,000 he might do business.

Now, I have in mind a little furniture company that manufactures furniture that needed $20,000 to carry on their operations, in order to fill their orders, ship their goods, and get them in a condition where they could collect their money. But the banks would lend them only $5,000. That was not enough. That would not pay their pay rolls for 3 months, and the carrying charges that they were running up. But they did find an individual who loaned them the $20,000 at a high rate of interest, and they took that loan and they manufactured their product and sold it, and collected for it, and today they are operating on a basis where their full necessity is a $5,000 loan on a 90-day basis.

So, in that case, instead of putting 70 men to work, they put 150 men to work, and I am just wondering whether or not—and I want to explore it thoroughly, and not go off half cocked—that principle, applied to business and commercial loans as we have applied it to building loans, would not get a lot of men to work at the present time that cannot find work, because these small businesses cannot get the money to finance their operations.

Mr. **Goldsborough**. Has it occurred to you also, and I am just thinking out loud, that that operation would tend to increase production, with no guarantee of distribution, and might ultimately cause a collapse?

Mr. **Ford**. If you increase production, you put men to work, and they are consumers.

Mr. **Goldsborough**. They are consumers, yes; but they do not get it all. When they are engaged in capital production, it does not all go in wages, and you have got to have a tremendous basis of commercial loans at the base of the pyramid in order to support your capital loans at the top. That appears to be true; but I am not undertaking to say that your plan is unsound.

Mr. **Ford**. Neither am I.

Mr. **Goldsborough**. These are just things that occur to me.

Mr. **Crawford**. Will Mr. Ford yield for a question.

Mr. **Ford**. I will be glad to, if Mr. Goldsborough is through.

Mr. **Goldsborough**. Yes.

Mr. **Crawford**. What you have in mind is that this would apply to loans to any extent at any time, for purposes other than increasing the flow of finished goods?

Mr. **Ford**. No; I would keep it on a pure commercial loan basis.

Mr. **Crawford**. Let me ask you, or Mr. Goldsborough, or both of you, if when you spoke of capital loans, you had in mind that goods in process are as much fixed capital as are plant and machinery?

Mr. **Ford**. No; I think that they are liquid capital, but not fixed capital.

Mr. **Crawford**. That is the point that I wanted to bring out, because it seems to me that when you think in terms of a building and machinery, and machine tools as related to finished goods, that the stream of in-process goods is as directly fixed as is the building and machinery, because there can be no finished goods in the absence of goods in process, any more than there can be any goods in process in the absence of finished goods.

Mr. **Ford**. Theoretically that is true, but there is this distinction, that if I were making a man a loan on his plant and machinery, I would probably make it for a long period of time, but if I were making him a loan of $100,000 on goods that he had in process of manufacture, I would want that loan to have some relation to the period that it would take to manufacture and market those goods.

Mr. **Crawford**. Is it not true that he can never totally liquidate the goods in process until he stops production? As a matter of fact, he cannot do it then, because there is no such thing as finished goods in process.

Mr. **Ford**. I am thinking of the flow or rhythm of goods produced, marketed, paid for, and new goods produced, marketed, and paid for; I am thinking about the circle that goes around. I am not offering it as a panacea or anything else; I am just offering it with the idea of having it explored by thinking men who have in mind some remedy for the situation in which we find ourselves. We have at the present time, it appears, something like 22 or 23 million men out of work. Probably two-thirds of those people could do some kind of useful work in industry or commerce, if industry and commerce were geared up to the point where they could be absorbed. We have always had that.

In 1929, as a matter of fact, we had 22,000,000 people in the country who were living at or below the subsistence line. We did not know anything about that at that time, for the reason that private charity took care of them, and public charity, in a way, but when we came to the panic they were dropped right into the lap of the Government and we found out about them. That number has been increased very much since we have taken up the slack in normal employment; but I am not criticising anybody, for it is just the system that we live under.

But it seems to me that there has always been a complaint from business, and small business particularly, that they could never get adequate banking loans——

Mr. PATMAN. Mr. Goldsborough——

Mr. FORD. Just a moment—and if the F. H. A. plan or principle were applied to commercial loans, and if you thereby only increased the commercial loans being made by the banks throughout the Nation 20 percent, it would be quite a bunch of money, and it would put quite a bunch of money into circulation and quite a lot of people to work. It may not solve the problem, but it seems to me that it is just a step in that direction, and I personally feel that the subject is worth exploring, and that is all that I am doing, to see what there is to it. I may be wrong; I may be haywire, but I would like to have it discussed by intelligent men, such as this committee is composed of, who have some conception of the economic forces that motivate this great Nation.

Mr. GOLDSBOROUGH. Have you finished, Mr. Ford?

Mr. FORD. Yes.

Mr. GOLDSBOROUGH. Mr. Chairman, I just wanted to insert in the record, with the committee's permission, a bulletin of the American Retail Federation, dated July 8th, which analyzes, for the purpose of its subscribers and the retail trade in general, H. R. 7188.

The CHAIRMAN. Without objection, that may be done.

Mr. PATMAN. I would like to ask Mr. Goldsborough——

Mr. GOLDSBOROUGH. Just a minute—and also a Kiplinger Washington letter, dated July 10, which discusses very largely the issues involved in this bill.

The CHAIRMAN. Without objection, they will be incorporated in the record.

(The bulletin and letter referred to by Mr. Goldsborough are reproduced below:)

AMERICAN RETAIL FEDERATION,
Washington, D. C., July 8, 1937.

BILLS TO REFORM THE MONETARY SYSTEM

Three bills have been introduced into Congress for the purpose of monetary reform. They are the Goldsborough bill, H. R. 7188, the Patman bill, H. R. 7230, and the Binderup bill, H. R. 7627. The Goldsborough and Patman bills are redrafts of previous bills introduced by the same Representatives.

The fundamental philosophy behind each bill is the same, namely, to stabilize the purchasing power of the dollar by so-called managed money. The methods to be employed are radically different.

Hearings begin today on the Goldsborough bill, before the House Banking and Currency Committee.

This bulletin consists of two parts: First is the view of the proponents of these bills concerning the monetary system and the weaknesses which these bills are seeking to remedy. Second is the remedy proposed by H. R. 7188.

THE DIAGNOSIS OF MONETARY TROUBLES ACCEPTED BY THE PROPONENTS OF THESE BILLS

In the views of the proponents of these bills the following analysis of our banking and currency system, and its effects on production and consumption, must be understood, and accepted as true, before the various remedies proposed can be understood.

What money is.—Money is defined by Webster as anything that has a conventional use as a medium of exchange or a measure of value.

Money as a medium of exchange is of two kinds. First is legal-tender money, such as paper dollars, silver, nickel, and copper coins. This class of money can be termed currency. Today in this country we have about $6,000,000,000 of currency—not enough to serve the business needs of the country. As a result we have the second form—bank check—drawn against a demand deposit in a bank. More than 90 percent of the volume of transactions of the country are done with check money. A check represents a credit in a bank. Transactions by check mean merely shifting credit from one bank to another.

Money as a medium of exchange then consists of currency and credit,

Money as a measure of value.—Money is also used as a measure of value. As such, like any other unit of measurement, it ought to be stable. But when we look at the history of the purchasing power of the dollar we see that the dollar is not and never has been stable. If we take the purchasing power of the dollar in 1926 as 100, we find that in 1920 its purchasing power was 60 and in 1933 it was 166. This variation is unfair to both debtors and creditors.

When the value of the dollar rises (that is, when prices fall) banks call in their loans in order to take advantage of the increased value of money. This act causes a shortage of money and sends its purchasing power even higher (that is, prices go still lower). The money called in is invested in long-term debt. That is, it is taken out of use in consumption and put to use in production. This act, in turn, has the effect of increasing productive capacity and brings about an increased supply of goods in a decreased market.

The source of money.—Banks manufacture money. They actually create demand deposits from notes which are secured by collateral, mortgages, or by intangibles such as the reputation and earning power of the borrower. A bank can lend several times the amount of its actual reserves, the exact ratio being fixed by law. This means that within wide limits banks can expand or contract the supply of money available to the business of the country. This ability of banks to expand or contract the supply of money has an important, direct effect on production, employment, and prices.

Uses of bank-made money.—Bank-made credit is put to two uses, commercial loans and loans for the purpose of building up capital investment. Commercial loans are used primarily in trade. Capital loans are used primarily in expanding the means of production. In order to reap the benefit of capital investment, the means of production must be fully utilized. Methods of production, however, have developed faster than our ability to buy the goods produced. Industrial development came first, and has absorbed an increasing proportion of money by building up capital investment at the expense of credit in commercial loans.

The effect of the increase in investment credit is twofold. First, long-term debt has risen in relation to productive wealth. Second, the volume of goods that must be taken off the market has increased.

The only way to liquidate the long-term debt is to add a definite percentage of it to prices. An increase in price, however, slows down trade and retards the movement of goods that must be taken off the market. The attempt to move the volume of goods produced by mass production led industry to set up the present elaborate system of installment selling. True liquidation of this long-term debt, however, can be accomplished only through savings which result from active trade in consumer goods. For that reason installment selling is only a temporary expedient. We have been relying on the consumers' market for liquidation of long-term debt, and when that market fails, as it does in a period of declining activity in trade, then a serious economic disaster results.

Summary.—The four main points which make up the diagnosis of the proponents of these bills, as to what is wrong in the monetary system are:

1. Banks can create money and expand or contract the supply of it at will.

2. The safest credit rests on the flow of goods from producer to consumer; and the nearer to the consumer the better the risk.
3. Too much money has been taken out of the channels of trade and put into the channels of production, which means we have a top-heavy structure which may fall under adverse conditions.
4. As a measure of value money is not stable.

THE GOLDSBOROUGH BILL

Purpose of the bill.—The purpose of the bill, as stated in the declaration of policy, is twofold:

1. To adjust and control the price of commodities sold at retail so as to make it conform to the volume of purchasing power in the hands of the public.
2. To regulate the purchasing power so that production of wealth in this country shall be maintained in full measure.

The bill proposes to accomplish these ends by a discount in price on all goods and services purchased at retail. The idea has been likened to a national markdown sale, except that the retailer is not called upon to finance it.

Operation of the retail discount.—For the first 3 months the retail discount is to be 15 percent. Thereafter the rate of discount is to be set by the Federal Credit Commission, created by this bill, and is to be based upon the percentage which the idle productive capacity of the country bears to the total productive capacity.

For example, during the first 3 months merchandise at $10 would be sold to the consumer for $8.50. The retailer takes the cash he receives from the customer, together with a voucher to show that he has given the discount, such as a sales slip, to the bank. At the bank he deposits the cash and the voucher and receives credit for $10. The bank applies to the Terasury of the United States and receives $1.50 in interbank currency notes.

Interbank currency notes.—Interbank currency notes are to be distributed to the banks to act as the basis for the retail discount. After they have been applied to that purpose they are to remain as a circulating medium within the banking system and can be used in all clearing house and interbank transactions. These notes may be used by the banks as reserves, but not as a basis for expanding private credit in the form of loans built on fractional reserves, that is, banks may make loans based on interbank currency notes but only on a dollar-for-dollar basis.

Interbank currency notes are also made receivable for all forms of Federal taxation payable directly by the banks.

Regulation of money.—The regulation of the supply of money—currency and credit—is entrusted to two agencies.

1. The Federal Credit Commission (as created by this bill): The Commission by means of the retail discount puts new money into circulation. Whenever the Commission finds that an inflationary condition is tending to arise, it is to instruct the Secretary of the Treasury to call in interbank currency in a sufficient amount to establish and maintain monetary equilibrium. When notified by the Secretary, banks are to call in outstanding obligations in order to increase their reserve ratios. This will then permit the return of the interbank currency to the Treasury.
2. The Federal Reserve Board (as now constituted): The power of the Federal Reserve Board to conduct open market operations is continued. The power of the Board to raise and lower the amounts required for reserves is expanded, by allowing the Board to raise the reserve requirement up to 100 percent.

Aside from these two agencies, two provisions of the bill, already mentioned, restrict the amount of money in circulation. First is the provision which allows the interbank currency to be used only as a 100-percent reserve, and second the provision which allows the banks to use the new form of currency to pay all Federal taxes. These two provisions are intended to prevent an inflationary condition from arising.

Summary.—Inflation has been described as the result of making purchasing power (currency and credit) available to the public at a faster rate than goods are made and brought to the market. The purpose of this bill is neither inflationary nor deflationary, since the added purchasing power (the retail discount) is made available to the public only after the goods have been brought to the market and sold. The purpose of the bill, then, is to expand the supply of money in the country so that the Nation may utilize to the fullest extent its means of production without causing a period of inflation, and without causing a surplus of unsold consumer goods.

THE KIPLINGER WASHINGTON LETTER

THE KIPLINGER WASHINGTON AGENCY,
Washington, D. C., July 10, 1937.

DEAR SIR: Businessmen need to know what's wrong in the economic system, how to remedy it, what caused depression, how to promote stability.

It's a large order, and there are no easy simple pat answers. Still, there's such a thing as an attempt to see the basic situation, and an attempt to adjust particular business policies to the whole.

This special letter aims to give a bit of help.

Diagnosis by the Brookings Institution is well worth studying.—Brookings is a research body, independent, respected, generally accepted. Intensive studies since 1933 have resulted in a series of five books. They are "old stuff" to many, but they shed new light on issues of now. Findings and conclusions from these studies are discussed herein.

Government is being influenced by these Brookings studies.—Influence during next year will be greater than at any time in past. Eccles is in accord. Wallace is roughly in line. The President shows that he has been reading and adopting some of the Brookings ideas. There are inconsistencies and deviations in the Government attitude, but, still, it looks as if the views are progressively influential.

The "color" of Brookings economic and statistical researches.—Not "radical," not "conservative," as most people use these loose terms. Perhaps "liberal." . . . But Brookings men are essentially "scientific." They assume the capitalistic order, without arguing for or against it. They assume that it's the system with which we must continue to work. But they find many faults, and the faults are regarded as correctable. Like engineers' report on a piece of mechanism—an economic mechanism.

What's the production capacity of American economic machine?—Lump together all factories, farms, distribution agencies—everything. Eighty percent used, 20 percent idle at the peak of the last boom, 1929. About same proportion for past 30 years, on the average. About 60 percent used, 40 percent idle, at depth of recent depression. The above figures include agriculture. In manufacturing alone, the idleness was much greater.

Thus the economic machinery could produce more goods, could wash out the percentages of idleness as indicated, but to increase more than those percentages would require expansions or improvements or both.

As regards standard of living, the studies show that there's a physical limitation to early improvement in the standard of living. Improvement is limited by physical facts about the production machinery.

People just can't have more goods than the machine can produce.

But the main curb on higher consumption is purchasing power. Physical limitations on increased production might be removed gradually, but there would still remain the problem of mass income, mass markets.

Now, what are the facts about income of the millions or masses? Why didn't people buy and consume more, and thus "make more business?"

Here's why: Those who wanted to buy didn't have enough income. Seventy percent of families had $2,500 a year or less. They spent all or most for necessities. More than half lacked many actual "necessities."

What's a reasonable standard of living? What are necessities? Department of Agriculture has suggested standards. They appear to be "reasonable." To meet these reasonable standards for all families, we'd have to raise production by 75 percent. Compare this with the 20 percent of slack in system, 1929.

So—the economic machine at present can't produce enough goods to yield reasonable living standard to all. That's the physical aspect. But it could produce more than it does, if—if purchasing power.

Impressionistically, it's like this: The millions spend all for consumables, and could consume much more, if they had the income. The thousands spend only part of their income for consumables.

Fact: Income isn't divided among the masses in such a way as to make the greatest possible volume of business.

You are doubtless "rich," statistically "rich," among the 8 percent.

Only 8 percent of families had incomes of over $5,000, in 1929.

Only 2.3 percent of families had incomes of over $10,000.

Such families saved. The plus-$5,000 families saved some, and the plus-$10,000 families accounted for two-thirds of total savings.

Next step: Examine money savings, formation of actual capital.

Are all money savings used to construct new capital goods? And thus provide additional employment and mass purchasing power? Heretofore this has been assumed to be true, but now the Brookings studies demonstrate that it was not altogether true in the boom period of the 20's. Facts show not all money savings were used in constructing new plant and capital goods. The volume of productive financing was very much less than the volume of money savings available.

Here's what happened to the excess money savings in the 1920's: They were used in buying securities already outstanding, thus bidding up their prices, lowering "yields" on stocks. Situation stimulated issuance of investment and holding company securities, thus pyramiding shares on top of existing shares—without causing a corresponding increase in actual capital goods. Excess savings retarded progress and created speculative maladjustments—contributing to depression.

What caused the depression, therefore, was not overproduction, or even excess capacity, but rather the draining off of excess earnings into the hands of relatively few persons, the relatively "rich" persons, who dissipated their funds. This was not sole cause, but it was major. Some other causes: Credit excesses, unbalanced world trade relations, slump of farm prices, unstable public finance in some countries.

Apparently the key to business lies in consumer goods—goods made for direct consumption by people—the masses of people. Rate of growth of new capital is adjusted to, restrained by, the growth in mass purchasing power. Also, the extent to which existing plant is utilized is largely controlled by volume of consumer demand.

Should more saving be encouraged? Or less saving? The studies give no categorical answer, but emphasize two points;

(1) Historically, commercial bank credit expansion has overcome shortages of investment money.

(2) At present stage of economic development the primary need is for a bigger percentage of an increasing total of national income to be spent for consumption goods.

What's needed now along the lines of adjustment of income?

It is assumed the people need more goods and more services.

This calls for modification of flow of income to various groups so that they may buy the things they need and want. (This is opposite of the crop curtailment of A. A. A., and the output restrictions of N. R. A.)

Not mere "sharing of the wealth", Huey Long style, because actual redistribution of the country's wealth is physically impossible, for it is mostly in land, buildings, and plants. And a mere per capita division of current income is not sufficient; it is inadequate in amount.

Instead—increasingly wider distribution of income is needed, accompanied by an expanding volume of total income.

Taxation alone to force wide distribution of existing income is only a small part of the answer, for tax money is not usually employed to produce more consumer goods and services.

Public works and work relief are mere alleviating crutches, for they usually add little to the average general standard of living.

The constant effort should be to reduce prices, not raise them.

Increased money wages expand purchasing power only if prices are not advanced at the same rate.

It is the ratio of prices to wages which is important.

Farmers and workers: Higher wages, unless accompanied by low prices, tend to penalize farmers, who make up 40 percent of the population, thus causing maladjustments in purchasing power of industrial and agricultural groups.

The how, the what-to-do, the problems of recovery: Industrial output is still about 15 percent below the 1929 level, allowing for growth of population. Serious elements of instability and uncertainty remain, despite recovery thus far.

Favorable long-range factors are these:

Cheap plentiful credit, progress in liquidation of private debt.

Balance between wages and prices (in the recent past), and between agriculture and industry, has been reasonably well achieved.

Monetary and banking uncertainties have been lessened.

Foreign trade prospects are greatly improved.

Great accumulation of deficiencies in durable goods production constitutes a basis for large expansion.

Unfavorable long-range factors are these: Lack of balanced budget, and threat of inflation; recent signs of too-sharp wage raises and shortened hours; indications of new regulatory legislation which would bring new uncertainties and confusion; highly unstable and threatening international situation.

The Brookings ideas of a program for further recovery:

Federal budget: Balance it.

Gold: Keep a fixed price, work toward stable foreign exchanges.

Trade barriers: Reduce them, extend reciprocal tariffs.

Price reductions: Work toward them as a way to benefit from technological progress; keep wages and prices in proper relations.

Curtailment of production: Avoid all devices and practices for curtailing production, both in industry and in agriculture.

Work hours: Maintain them at substantially the present level, as the only means of producing the volume of goods and services required.

The future: Several years of great prosperity should be ahead as outgrowth of deep deficiencies in production accumulated since 1929. Theoretically this catch-up prosperity period will take about 5 years. Theoretically it will require the labor of 8 to 9 million workers in addition to those now employed, working average of 43 hours per week.

Even such a schedule would do no more than restore the standard of living equivalent to that of 1929.

To raise the standard of living above 1929 will require much technological advance, and great increase in efficiency. Whether we shall catch up depends upon policies, governmental and private.

Events of the past few months are regarded as worrisome. Prices have risen too fast, due partly to too-sharp wage increases without corresponding increase in efficiency. This is a combination which is apt to lead to a dangerous spiral of inflation.

This getting-out-of-balance is the biggest single threat to sustained recovery.

The preceding condensed discussion of the Brookings findings may serve as a sore of measure stick by which to judge various policies or issues now prevailing in business, political and labor spheres.

It's not propaganda for any pet cause in any of these spheres. The fact-finding and diagnosis are honest. The suggestions for remedies are controversial, but they represent straight reasoning from the facts. You may agree with some and disagree with others.

We act as reporters of the ideas, not as sponsors.

More complete discussions are in the five books themselves: (1) America's capacity to produce; (2) America's capacity to consums; (3) formation of capital; (4) income and economic progress; (5) the recovery problem in the United States.

They are published by the Brookings Institution, Washington, or may be borrowed from most libraries.

Check on government: Government is now trying to assume prime responsibility for managing the progress of recovery. Will government be sufficiently wise and alert to maintain the proper balance?

In current developments there are both parallels and conflicts with the Brookings conclusions. These will be noted from time to time in future letters.

Yours very truly,

THE KIPLINGER WASHINGTON AGENCY.

Mr. PATMAN. Mr. Goldsborough, I understood you to say that you expect to propose an amendment to cure a criticism that I brought up against your bill a few days ago, about the paper work that would be involved and about the many inspectors that would be necessary in order to properly supervise the work. Is that right?

Mr. GOLDSBOROUGH. No. What I said was—and I think probably you were not in the room——

Mr. **Patman.** I was here shortly after you started, and I thought I heard you say that you could offer an amendment to the bill that I understood would cure my objection, so that there would be no papers required.

Mr. **Goldsborough.** It was not your objection that I was referring to, but——

Mr. **Patman.** Regardless of whose objection it was——

Mr. **Goldsborough.** Just a minute. The objection that I had reference to was an objection which I have received letters about and which I have been concerned with myself, and that objection was that the consumer, if he was required to give a receipt every time that he made a purchase, when the discount was reduced, for instance, it would cause him to be displeased and create a difficult situation. That was the reason that has been suggested to me why an amendment should be made to the bill, and that is my reason. As far as the bookkeeping which you mentioned is concerned, that does not disturb me at all.

Mr. **Patman.** You would expect then to go ahead then and sign vouchers and things like that?

Mr. **Goldsborough.** Not if the bill were amended. The bill could be, in my judgment, amended in such a way that the inspector for the Federal Credit Commission and the retailer could work out the amount of the discount which the retailer should be allowed without the interposition of the consumer at all.

Mr. **Patman.** Without his signing anything?

Mr. **Goldsborough.** Without his signing anything. I believe that it could be done and worked out practically; yes.

Mr. **Patman.** Wouldn't that open the floodgates for fraud on the part of some of the one million and a half retailers in the country? Suppose that the Government man goes along and inspects John Doe's books, and John Doe says, "I am entitled to $60 discount here from John Smith. John Smith was in here and made a $400 purchase," and the Federal inspector would say, "Well, have you anything to show for it?" John Doe would say, "No; but he came here and I made the sale, and I am entitled to that $60, and I want that interbank currency," and the inspector could not deny it; there would be no way to disprove it, and it occurs to me that a plan like that, with a million and a half retailers in the country, would require a lot of Government men to keep up that inspection work, and would open up the floodgates to all kinds of possibilities of fraud. I just cannot conceive of a plan like that that would work out, Mr. Goldsborough.

Mr. **Goldsborough.** Do you think that it would be any more difficult than the collection of a sales tax?

Mr. **Patman.** A sales tax is where they collect something for the Government, or the State, and although they do not give it all, they probably give part of it, or substantially the amount that they have collected, but here is a case where all they have to do in order to get money out of the Government is to certify that "I sold So-and-so $100 worth of goods, and he bought them for home consumption, under the terms of this law, and I am entitled to have 15 percent discount."

Mr. **Goldsborough.** It seems to me, Mr. Patman, that if the proper criminal penalty were involved in that sort of fraud, and also the discontinuance, for the punishment of the indicated retailer, of the right to give the discount in the future, he would hesitate a long while before he would engage in that kind of fraud, because it would soon put him out of business.

Mr. **Patman.** I know, but you have to make out a case, and whenever you allege something against a retailer, you have to prove it. He says, "I am entitled to this $60. I sold John Smith $400 worth of goods, and it comes within the terms of that law, and I am entitled to that 15 percent of interbank currency," and the Government man could not deny that. He would not even be able to find John Smith.

Mr. **Goldsborough.** He would find some of the "Smiths" before long, in my opinion——

Mr. **Patman.** And it occurs to me that if you establish——

Mr. **Goldsborough** (continuing). And the one Smith that he found——

Mr. **Patman.** It would just open up the floodgates——

Mr. **Goldsborough** (continuing). That had engaged in the practice that you referred to would be put out of business for all time, because he would not be permitted to use the discount.

Mr. **Patman.** I know generally that retailers are honest men and want to do the right thing, but I would be very reluctant to give them all a checkbook on the Government, for it occurs to me that that would be the same thing, if you told them all, "You do not have to get the man's name."

Mr. **Goldsborough.** Oh, no; I did not suggest that the retailer would not have to furnish the agent of the Federal Credit Corporation with that man's name.

Mr. **Patman.** I thought you said that he would not be involved in it.

Mr. **Goldsborough.** I said that, in my opinion, in order that this law might operate properly, the consumer himself would not necessarily be required to give the retailer a receipt or a voucher.

Mr. **Patman.** All right. Suppose that you are the prosecuting officer, and you are investigating this case. This retailer says that he sold $400 worth of goods to John Smith, but you say that you doubt that. He brings John Smith, and he swears to it. The two of them get together. How would you dispute that?

Mr. **Goldsborough.** Of course, Mr. Patman, if you get enough liars together, I guess you can beat anything.

Mr. **Ford.** Did you say liars or lawyers?

Mr. **Goldsborough.** I was speaking of liars.

Mr. **Ford.** Both liars and lawyers, I guess.

Mr. **Crawford.** Does Mr. Patman yield?

Mr. **Transue.** I object to that, even said facetiously. I am a lawyer myself——

The **Chairman.** I am sure that the gentleman will make the proper correction in the record.

Mr. **Crawford.** I want to ask Mr. Patman a question.

Don't you think that the mechanics of that can be handled as easily as they handle a mark-down in these big department stores from an income-tax standpoint?

Mr. **Patman.** If they did not have anything more than department stores to deal with, that would be all right, but you have a million and a half retailers all the time.

Mr. **Crawford.** But I am discussing the principle only, and you are directing your remarks to the volume.

Another thing that would happen under a plan of this kind would be that the retail discount would universally become effective throughout the entire United States, at a given opening day of business, we will say—in other words, on July 21, a certain discount begins to operate. So that I think the mechanics of it would not be so bad. Of course, it will call for a lot of high-grade bookkeeping.

Mr. **Patman.** I just expressed the hope to Mr. Goldsborough that in considering amendments he would consider one that would strengthen that part. It occurs to me right now that, with a million and a half retailers, it would take at least one Governmeent man for each retail place to supervise it and to protect the Government, and the Government has to be protected. You cannot just let the retailer say, "I am entitled to 15 percent," in order to get it. Then it would take extra help in each store to keep these books, and extra help in these banks to handle all these vouchers and receipts. So, unless it is changed, it will take 10,000,000 people.

Mr. **Ford.** Are you not contemplating a situation in which the moment this bill went into effect there would be a 15-percent discount on all goods and services?

Mr. **Patman.** No. It is more confused by making it just applicable to a number of them. It requires more bookkeeping to keep them separated. If applied to all, it would be more simple.

Mr. **Ford.** Would it not resolve itself to this, that if the whole commercial and industrial field in the United States produced on the one day $200,000,000 or a billion dollars worth of goods, those goods would immediately go into circulation at a 15-percent discount?

Mr. **Crawford.** This would be a retail transaction.

Mr. **Ford.** Yes; that is right, and the Government would make up the difference between the fixed price and the price sold. I do not know where the Government would get off, so far as paying the bill is concerned.

Mr. **Patman.** And I do not know what is behind this money either.

Mr. **Crawford.** It seems to me that the money situation could be remedied easily by an amendment or provide that all of these transactions be handled by bookkeeping entries, and keep entirely away from the interbank currency; drop it out of the picture.

Mr. **Patman.** Drop the interbank currency out of the picture?

Mr. **Crawford.** Surely.

Mr. **Patman.** Who will pay the 15 percent?

Mr. **Crawford.** It will be absorbed through your bookkeeping entries.

Mr. **Patman.** But somebody has to be behind it.

Mr. **Crawford.** The thing that I am mentioning which will get us away from that psychological fear that you bring up is that that could be met entirely through bookkeeping entries, but keep entirely away from the issuance of any type or kind of currency.

Mr. **Patman.** You cannot run a business purely and solely on bookkeeping entries. Pay day comes around, and somebody has to pay.

Mr. **Crawford**. I understand that, but all that I am talking about is having bookkeeping entries between your company, say, and mine, without transferring any money between us.

Mr. **Patman**. What is the gentleman's understanding as to what is behind this interbank currency, who is guaranteeing it, and who will pay it?

Mr. **Crawford**. The only guaranty that I see behind it is the actual production of goods.

Mr. **Patman**. But the goods have already been sold. The goods were sold before the currency was issued.

The **Chairman**. Without objection, we will resume the hearing tomorrow morning at 10:30 o'clock.

(Thereupon, at 11:50 a. m., an adjournment was taken until Wednesday morning, July 21, 1937, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

WEDNESDAY, JULY 21, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Messrs. Goldsborough, Reilly, Williams, Spence, Ford, Brown, Patman, McKeough, Evans, Transue, Wolcott, Luce, and Crawford.

The **Chairman**. The committee will come to order.

Gentlemen, we have with us this morning Mr. Harvey, who was introduced to you yesterday. We will be glad to hear from you, Mr. Harvey. Will you give us a little of your history and background for the record?

STATEMENT OF EDWARD F. HARVEY, OF GWYNEDD VALLEY, PA.

Mr. **Harvey**. Mr. Chairman, I was educated as an engineer, but as soon as I left college I went into executive work, productive work, and I have been at that for 40 years. Later on in life I became interested in banking, and became a very considerable shareholder in banks, and a director, and that brought me into contact with the relationship between industry and finance, capitalization and income; and when the crash came, my bank stocks withered, as we know those of everybody else did, and I set to work to try to find out why, I having retired, most of my interests having been merged with larger concerns, and I was free, so I went to work and from an engineering standpoint tried to find out what had become of my money, and the result of it, part of it, is what I hope to present to you this morning. Does that cover it?

The **Chairman**. So you bring to the committee some of the lessons you have gathered in the school of experience?

Mr. **Harvey**. Yes, sir.

The **Chairman**. We are very glad to hear you, and if you have a prepared statement, which I believe you indicated yesterday to be the fact, you may proceed and the committee will not undertake to interrogate you until you have finished with your prepared statement.

Mr. **Harvey**. Thank you, sir. That is very satisfactory. I would like to express my appreciation to you and to the committee for hearing me on this subject. It is one that I feel very strongly about.

The statement made by Mr. Goldsborough on the 8th instant, before this committee in explanation of the purpose and technique of H. R. 7188, covered the economic essentials upon which it is based.

As a believer in these essentials, I have pleasure in presenting a few supplementary points for your attention.

Mr. Goldsborough then said that the primary objective of his bill was to equate within a reasonable margin the consumptive and productive capacity of this people. He revived with emphasis, the principle of the flow of commercial credits through the banking system as being the monetary equivalent and economic force upon which such an industrial balance is necessarily founded, and showed how this bill is designed to achieve that end.

As I interpret them, the provisions embodied in it are based upon monetary and economic fundamentals that have been historically proven, and the only striking innovation is the extension on a national scale of the principle of lowering prices to induce sales, and the use of the Federal monetary power to provide the necessary credits, without enhancing Federal indebtedness.

Otherwise every link in the financial chain has been in daily use for half a century, including the revival of an old monetary principle that has been gradually slipping into the discard for some time past. That principle is the predominance of the commercial credit for moving goods in excess of all other forms of bank credit in any sound monetary system. You cannot have a sound monetary system built upon bank credit without it. And you cannot express national capital wealth in real dollars or give savings a sound dollar value without an even flow of these commercial credits.

I understand Mr. Goldborough's use of the phrase "commercial credit" to mean not only the circulation of commercial loans and acceptances representing goods in course of distribution, but also the flow of checks which represent transactions of a similar nature liquidated by cash payments. The volume of the latter form of monetary transfers representing goods passing into use, has been increasing for some years, and banks get little or no income from this type of transfer. But the principle of measuring the flow of goods by this flow of monetary tokens representing them, whether of deposits arising from loans or permanent cash deposits, is essential.

In the case of the type of Government financing that has been recently current, whereby permanent money is put into circulation through Federal borrowing, the public pays the bankers' costs through taxation to meet the cumulative interest charges. In the type of financing proposed in H. R. 7188 the individual business taking advantage of it, pays a flat noncumulative service charge. This service charge helps restore income to the banks which the Federal Government is now paying them in the form of interest, irrespective of the volume of goods that flow as the result of it. As the flow of goods increases under the incentive of lower prices due to the retail discount, this income should increase correspondingly.

On the basis of the $15,000,000,000 that the Government has put into circulation in recent years, and which was primarily designed to increase the production—consumption volume—the national income should have increased about 40 billions and should now be approaching $100,000,000,000 or to a parity with 1929, allowing for the increase of population since then.

As to the distance along this road that we have already come, it is misleading to compare gross annual income without adjusting for real income. In other words, a correct estimate should allow for the relative increase of the general price level and the dollar volume of income.

The statistics record a national income for 1933 of about $40,000,000,000 and for 1936 about 63 billion, or an apparent increase of about 60 percent. But the price rise index is from 64 in 1933 to 81 in 1936, or 25 percent. Therefore, the real income in 1936 would be around $50,000,000,000, based on 1933 dollars.

The 1929 real income based upon a similar price level that existed in 1933 would be 29 percent less than that recorded, or about $60,000,000,000. So that it appears at the end of 1936 we had come about halfway toward the actual 1929 income. Since then we have come somewhat further but more Federal money has been put into circulation on the basis of a steadily rising price level. It is scarcely possible yet to ascertain what the real income of 1937 will be. It has been estimated on the current dollar at about $75,000,000,000. On this basis the real income for 1937 on a 1933 dollar valuation would be somewhere around $60,000,000,000.

The real income this year, therefore, would be close if not equal to that of 1929 on a 1933 dollar. But it would be about 9 percent less per capita on the basis of population.

It has cost about $1 of new Federal indebtedness to win $1 of increased real income. In other words, the increase of Federal debt by 20 billions has resulted in about 20 billion dollars increase of real income.

Viewed from a financial angle, this does not appear to be an adequate result for 20 billion dollars of new Federal debt. The new method of financing the consumer, proposed in this bill, is designed to provide a more efficient use of national money without adding to national debt and debt charges.

Recent statistics of the Federal Reserve Board and Department of Commerce show that private deposits in banks have increased about 15 billion dollars during the time under review, and that private long-term debts have been reduced about 10 billion dollars, of which 9 billions are urban real estate and 1 billion railroad indebtedness. At the same time the savings in mutual and postal banks have remained about stationary.

These figures also show, first, that the Nation has assumed 10 billion dollars of private debts, while increasing its own indebtedness 20 billion dollars and that the rest of the money has drifted into large bank accounts, where it does not fully serve as buying power for the mass of the population as it was intended to. That is the reason that we have to go on and on and on with Federal indebtedness.

There is another element that enters forcefully into the objective of this bill. It is the mounting deferred payments on the purchases of consumption and semidurable goods. There is no absolute measure of these as yet, I believe. But they have been estimated at anywhere between 6 and 14 billion dollars. They are taking up the shortage of buying power as against goods produced. But as soon as the buying public stops buying goods on time payments and starts to tighten its belt and liquidate them, it is an absolute certainty that production and income will decrease, and with them the burden of long-term debt will begin to press downward again with increasing pressure, because in point of actual fact, nothing has been done to liquidate it. It has been merely a transfer of debt, private indebtedness to public indebtedness.

The inescapable conclusion is that if you have an overgrown debt structure, no matter whether it is private or public, and in our case it is both, the only way to liquidate it and bring it into controllable proportions is to create more wealth increasingly without going into new debt and to do it by holding the price level of consumable goods at a point that will assure increasing production.

It was only last February that this committee heard Mr. Marriner S. Eccles testifying in favor of broadening the base of collateral for the issue of Federal Reserve notes. His reason was the danger of further drastic liquidation following a speculative demand for increased bank credit.

It is difficult to see how further extensions of long-term credit on top of the already frozen mass of indebtedness can prevent the eventual toppling of the debt credit structure, although it may postpone it. Presumably, the idea behind this recommendation is to assure the banking system a longer breathing spell. But will this be any real advantage in the absence of the means of the orderly liquidation of the 130 billion dollars of debt outstanding?

Thus the actual results of the policy of raising national income and the price level simultaneously, that we have been witnessing, support the arguments given above and form the fundamental philosophy of H. R. 7188.

This brings me to the vital point of this whole problem, namely, the absolute necessity for noncumulative consumer credit. I emphasize the word "noncumulative" as against installment selling. We have seen that the increase in Federal debt has resulted in the repayment of private loans amounting to 10 billion dollars, and the increase of private deposits of 15 billion dollars, the cost of which the American public as a whole is saddled with, not only for the principal sum, but for debt charge accruals, for an indefinite time in the future.

Suppose, however, that national income is raised, without raising the price level of consumer goods; the direction of the flow of new credit would be changed. It would tend to remain in circulation as buying power instead of drifting too rapidly into capital credits and reserves.

The reason for this is to be found in the way money behaves when there is a crushing overplus of private debt, and when there is no definite assurance that the demand for funds in trade is fundamentally stable and sound.

Again, looking at our statistics, we find that the apparent rise in national income and the actual rise in the commodity price level brought about a more active demand for investments. Many debtors who were holding backlogs of depreciated securities found that the advance in securities placed them in a position to realize and liquidate their indebtedness. It is highly significant that the decrease of long-term debt was nine-tenths urban real estate, which represented almost half of the frozen indebtedness, and in which probably the most aggravated abuse of the extension of credit occurred in the previous years.

This reduction took a great deal of the new Federal money out of circulation, and extinguished it or transferred it to the bank accounts of entrepreneurs. It may be pointed out in following these thoughts through, that when Federal money is paid out, its first effect is to stimulate buying power. It buys and pays for goods and this increases the cash balances and working capital of businesses of all classes. And the first thing these people want to do is to relieve the pressure of their debts. The same thing, of course, applies to all sorts of services. They reestablish their economic security as far as they can by a species of forced saving which takes the money out of circulation as buying power.

This cannot happen in the same degree if the Government credit is applied in the way that H. R. 7188 proposes. First, because the lowering of prices offsets any withdrawals that will occur and second, because if they do occur in excess and stagnant accumulations of money curtail the volume of circulation, that money can be called in and again applied to the maintenance of low prices for goods in demand. And, thirdly, because there are no debt charges and accruals to cause further reductions in circulation, higher taxes and prices.

Another important factor is the fact that the increased flow of goods brought about by the lowering of prices results in real income and real wealth, and strengthens the credit base so that savings become real savings, and not monetary tokens of doubtful dependability. In addition to this the additional flow of goods would require the retention of larger amounts of working capital in business and consequently in circulation; and prevent the forced savings for the use in relieving the pressure of debt. The increased volume of business would tend to relieve this pressure, and result in liquidation that would be fundamental, namely, as the result of the increase of real wealth, not of price rises.

According to current statistics we are now producing new wealth at a rate close to if not equaling production in 1929 on a price level about 10 percent lower and on an employment schedule about the same as 1929, without allowing for the increase in population. This is to the good as far as it goes, but two points must be considered. One is that the Federal Government is still supplying about 4 percent of the money to buy these goods, and deferred payments and installment selling is accounting for another 5 to 6 percent. Some authorities place this figure very much higher. But it is certain that there is a shortage of buying power of about 10 percent of the amount necessary to distribute production on a pay-as-you-go basis, at the present time.

The Brookings Institution investigation indicated that the withholding of savings, chiefly in the higher-income brackets tended to make a chronic shortage of this character. Mr. Goldsborough, in his address on Thursday last, quoted extensively on this subject, so it seems unnecessary for me to go further into detail. This condition is one of the warrants for the proposals contained in H. R. 7188.

It must be remembered that a shortage of buying power of this nature is cumulative, and adds constantly to the debt burden as well as reducing spending power later on. A 10 percent shortage would be a fifty percent shortage at the end of 5 years, which is about the time that many economists allow for the turn of the business cycle. I would like to say in parentheses there that of course I do not figure there will be an actual accumulation of 50 percent in 5 years if there is a shortage of buying power of 10 percent a year, because there are so many factors that come in. One is raises in salaries, another is the result of the distribution of estates of others, and various other sources of income, such as increase of business through prosperity—all of these things would tend to speed up liquidation of this indebtedness, so that the 50-percent shortage would not exist. But what I want to illustrate is the way it works, that that shorage is accumulating all the time, and that when some other cause brings about a downward movement, that is just another pressure to accelerate it. It all adds into the steady increase of indebtedness.

Statistics indicate that long-term indebtedness increases at the rate of between 8 and 10 percent per year on an average and that national productive wealth, if not disturbed by intense depressions, increases 3 to 4 percent a year. It should be perfectly clear that this cumulative condition must inevitably spell the complete breakdown of capitalism as we know it. I think that that is beyond argument.

By the way, those figures are definite figures. On the increase of wealth, Dr. Snyder, of the Federal Reserve Bank, made very exhaustive analyses of the average increase of wealth in the United States on a stable dollar, and he makes it from 3 to 4 percent, and a number of other economists have got more or less the same result. The matter of indebtedness and the increase in indebtedness is a matter of plain figures which can be got from the Department of Commerce records and the research of Evans Clark on the internal debts of the United States. Those are very authoritative sources.

By permitting and fostering this tendency, free capitalism and industrial democracy are destroying themselves with certainty. This is the reason why I as an individual feel that the problem is one for capitalists and bankers who believe in the democratic institutions they have inherited jointly with the Nation as a whole.

I would like to say a few words about these problems in relation to taxation. As things stand at present, the total long-term debts of the country consist of the following: Private, corporate, and industrial, 75 billions, which has been reduced from 85 billions in 1930.

Federal 31 billions, increased from 16 billions in 1929.

Municipal, State, and local, 17 billions, making a total of 128 billions.

To this should be added short-term debts of all classes, 100 billion, making altogether 228 billion.

At the present time national wealth may be variously estimated at 250 to 300 billions. Not a very wholesome condition from the banking standpoint. The margin of wealth to debt is a little bit small for sound banking purposes. We can liquidate it to a point where the statement will be sound enough by getting busy making and selling the goods we are equipped to produce, and for which there is an ample market. If we were shipping our goods abroad we would finance the exports. Why don't we finance our home markets, which are so near to us?

The point I want to make in connection with taxation is this, that any form of debt is a tax upon industry that is reflected in prices and the cost of living. There is really no difference whether the debt is incurred by private enterprise, or through governmental authority; the tax upon industry is the same. It is probable that Government debt is the least onerous because of the lower cost and because the liquidation of it is likely to be less pressing.

The cost of money to Government is now about 2.72 percent, and for private indebtedness about 5 percent. The total interest charge on the latter is estimated by the Department of Commerce at 4.1 billion dollars per annum without amortization charges. This is almost equal to the whole Federal revenue.

It may be assumed from these figures that the tax rate on private debt is far higher than the tax rate on public debt. It is also probable that the revenue from Government debt finds far better distribution as buying power than the revenue from private debt. So that it appears absurd for those who are responsible for this great burden of private debt to point the finger of scorn at the Government's fiscal policies. It seems to be a case of stones and glass houses.

The way out is cooperation to mitigate both forms of debt and reestablish the working of a free economy. The way to mitigate them is to increase production and consumption without adding to debt.

I would like to say something about fundamental economic law. The law of supply and demand is probably the most fundamental of them all. It has existed as long as the human race. And long before there was any thought of money, demand or need gave rise to supply.

But with the advent of money and credit a new factor has been introduced by human agents that has nothing to do with the fundamental law. It is effective demand, a purely monetary factor which has been steadily losing any relation to the basic demand factor of the law. Money and the ability to get money have been substituted for the fundamental factor of true demand. Any one who tries to set up an arbitrary factor in place of a natural factor in the interpretation of natural law is bound to cause trouble and error. Nevertheless, our economists have substituted a monetary factor to represent the great law of demand and supply and have refused to consider any other. Any scientist knows that he cannot monkey with natural laws that way. Are economists lacking in a similar intelligence?

Under H. R. 7188 the arbitrary factor of effective demand is made to reflect the fundamental factor of physical demand.

Regarding the technique of this bill, I will not attempt to go into details. But I would like to say a few words in explanation of the interbank currency it proposes.

National currency, as at present issued, cannot be legally recalled except by taxation. This currency is almost entirely issued as a debt. In other words, it is virtually sold to the banking system. By making repayment of the currency to the Treasury, or Comptroller of the Currency, banks can relieve themselves of the obligation which they incur when they call for currency, and for which they pay in one form or another.

In the case of the interbank currency the transaction is entirely different. The currency is advanced to the banks as a base for the regulation of credit. It is created and issued for the purpose of regulating the money of the country in relation to the supply of goods. It has no connection with transactions involving capital.

If we compare the issue of this currency with a private transaction of the same nature, perhaps the answer may be clearer.

If I deposit a $100 Federal Reserve or Treasury note with a bank, the bank holds that note on call. But it issues credit for its own account against it to other customers.

When I withdraw that deposit of $100 the credit base of the bank is reduced by that amount. The bank would automatically recall some of the credit they had issued to their customers so as to restore their own credit.

What applies to my $100, of course, applies to the millions of other transactions of a similar nature which make up the bank-credit system.

If the Federal Government entrusts to the banks a deposit to be used for a specific purpose which can, if necessary, be written on the face of the currency notes, the situation should be the same as when a private depositor makes a deposit.

In 1929 billions of dollars were entrusted to banks to loan for private account—loans for account of others.

The control of money that H. R. 7188 proposes through this currency is the nearest approach to the constitutional provision that has so far been devised. It simply carries the existing system one step further up and into the hands of the national monetary authorities.

Now, if I may be permitted to, I should like to make a few comments upon the hearings before this committee in relation to the Banking Act of 1935, especially in reference to some points brought out by Governor Eccles. Have I that permission?

The **Chairman**. Yes.

Mr. **Harvey**. One of these was the emphasis laid upon the distribution of spendable income. It was pointed out that the Government's policy was directed toward that end and had furnished large amounts of money to influence it. But the difficulty was and is to maintain this circulation under the method of trade credits for production.

The Governor used an apt illustration when he said that you could not push a string. That banks could not push money out for commercial loans unless the demand justified it.

This is obvious, but the logical answer is to pull the other end of the string. Only the public can do this if they have the means. This is where Mr. Goldsborough's bill comes in. It gives the public the ability to pull that end of the string.

Another point that was stressed was the importance of speeding up the velocity of money as a prime factor in trade revival. May I express the opinion again, that the prime factor is not the velocity of money in itself but the speed of revolution of money that represents the transfer of goods. In other words, the cycle of trade credits and debits.

The velocity of money is not geared directly to the production of wealth. It has an indirect influence upon it, but it is not geared closely enough to be a reliable factor. And it frequently varies in a contrary direction to production and distribution. It is influenced more by the trend of prices, either up or down, than by the actual production of wealth.

In the first place, millions of transfers of money take place that do not represent the transfer of goods. This is true both in the spending of income and the trading in capital values or commodity holding, hedging, and speculation.

H. R. 7188 is, therefore, based on monetary transactions involving the actual transfer of goods, as the fundamental monetary factor.

One of the points that was brought out clearly in Governor Eccles' testimony is that there has been an important change in the relation of the power of Congress and the Government over the control and technique of the monetary system. It is now clear that by a method of cooperative borrowing from the banks, far beyond any possible open market capacity, and at very low rates of interest, a system of national money has been established which assures greater stability to the money supply. In passing, it might be remarked that the word "borrowing" to express current fiscal transactions may be regarded as a misnomer.

It seems to me that the weak spot in this system is that this money does not give a sensitive enough control of the credit base, and this has been virtually admitted by Governor Eccles in the statement that inflation may be far more easily controlled than deflation by the present set-up.

May I point out that the chief cause of forced deflation is the pressure and overburden of debt and debt charges and is largely a matter of price trends. It was generally admitted at the hearings that price-level control by any method except through credits would not work. By which I mean that price control by legislation would be unworkable. It would be destructive of our existing economic system. On the other hand, if you can pull this credit string from both ends and abandon the idea of pushing it, you introduce an element of price stability for commodities which will give added stability to all other financial transactions, especially that involved in the liquidation of debt.

It was brought out in the discussion of Governor Eccles with Mr. Cross and Mr. Clark that besides the control of the volume of money, two other elements were needed to give control of the velocity of money. In reply to Mr. Clark's question that in his previous testimony Governor Eccles had given a tax system and a program of Government spending as the other elements, the Governor said, "Those are the two elements which it seems to me in our capitalistic economy, must be taken into account to bring about a sufficiently equitable distribution of the national income to keep up full employment, full production, and keep the production facilities adjusted in relationship to the buying power of the Nation."

To me personally, this is a very wise and true statement. It embodies the fundamentals upon which H. R. 7188 appears to be built. The bill connects directly with the third element in Governor Eccles' program, namely, Government spending. It meets the two obstacles to the above program named by the Governor, namely, wider distribution of the national income by natural means, and control of the volume and flow of money into the channels where it is needed.

But it goes somewhat further toward the ultimate solution of a balanced economy by giving the central monetary authority, wherever it may be lodged, an additional direct lever for credit control and changes the trend toward increasing debts to a condition under which orderly liquidation may be achieved through the increase of real wealth. It thus makes room for the financing of new wealth which is pressing for development, on a monetary base closely related to intrinsic values.

In the matter of taxation, it simplifies and eases this element and gives a rational basis for equitable tax adjustments, that must be used in any free profit economy to maintain a monetary cycle in harmony with production and consumption.

I would like to emphasize again the importance of realizing that the increase of long-term debt in excess of the increase of real wealth, which has been occurring, and which seems inherent in our financial system, is perhaps the greatest obstacle to a balanced monetary system that exists.

This excess of debt intensifies the drift of money out of the channels of trade and so reduces the means of payment. If there is a relatively low ratio of debt to productive wealth, it is possible to compensate for this loss of buying power by increasing the debt burden gradually, and this is exactly what has happened to us. But when the debt burden reaches a certain point, and I think that point has now been reached, further increases in debt only aggravate the situation by intensifying the periods of forced liquidation, which Governor Eccles has called to your attention.

To get out of this impasse it is surely necessary to increase purchasing power to a point where debts can be liquidated out of the increase of real wealth and not by going deeper into debt. H. R. 7188 attempts to show how this can be done. Thank you.

Mr. FORD. Might I ask Mr. Harvey one question?

Mr. Harvey, let us take an example of an automobile that has a fixed cost value at the factory, we will say of $1,000. It has a sales value when it gets here of $1,500. I am giving arbitrary figures, of course. Now, on a rising market, might it not be conceivable that the dealer would jack his price up to $1,800, because he thinks that he can get it, because he thinks that the law of supply and demand warrants his raising his price $300 and making an extra profit? Then, if he found, after doing that, that he could not market the machines that he had, he would cut the price 15 percent, we will say, which would be $270, and bring it down to practically its original sales value. Then, if the cars moved at that figure, he would still be, as far as his profit was concerned, where he would have been in the first place, with probably a few dollars added.

Mr. FORD. Do you think that the Goldsborough proposal of a 15-percent reduction at that point would be effective in causing that flow of goods to start?

Mr. HARVEY. Yes; I think it would. It would make the man who had $1,500, we will say, to buy an automobile, enabled to buy the automobile, where he would not be able to buy it at $1,800, and furthermore, if he had decided to finance it, he would have to finance $280 less. That would be that much less burden on him. He would have that much additional margin out of debt.

Mr. FORD. So it would do two things: In addition to stimulating the market for that type of machine, it would also reduce the indebtedness that goes with installment buying just that amount?

Mr. HARVEY. Yes.

Mr. FORD. That seems to me to be sound, but there is just one other question, and that is with respect to the interbank currency. After he sold that machine on these figures he would go to his bank and say, "Here, I sold an $1,800 machine for $1,530. Therefore I am entitled to $270 credit on your books, to my account."

Would not that element be likely to enter into all the transactions? Would there not be a tendency on the part of the retailer to utilize that device to get the full price and still get a discount or a credit from his bank? I realize that if he were caught at it, he would be barred forever from entering the retail trade, but how could he be detected?

Mr. **Harvey**. How could he be detected if he raised the price?

Mr. **Ford**. Yes. He would say, "My overhead and my cost of doing business, and so forth, warrant my getting a $800 profit instead of a $500 profit."

Mr. **Harvey**. I do not believe that he could do it without being easily detected. Does not the competitive drive to sell automobiles influence his ability to raise his price? Would he not put himself out of business, or would he not lose the sale if he raised the price above the competitive level?

Mr. **Ford**. But suppose all of the dealers got together and said, "There is a big demand for these cars; why can't we get an additional $100?"

Mr. **Harvey**. Is that legal under the present law?

Mr. **Ford**. It is not legal, but it is done.

Mr. **Harvey**. I do not believe there is any way in the world of stopping chiseling, but I do believe that the majority of automobile dealers, and all of the larger and responsible businesses, would find it very inconvenient and would hesitate a long time before they went outside of their regular methods of business and regular price levels to chisel, and I am sure that if you had 20 dealers selling Chryslers in Washington, some of them would be honest enough not to do what some of the others might offer to do, and I think that you would have a public reaction to that sort of thing that would very soon put people inclined to do that on the spot, in the same way that they lose out if they try to do it today without any discount.

Mr. **Ford**. We have always depended on the competitive system for regulating business, but it has not been so tremendously effective. With such raw commodities, for instance, as rubber, we know that it has failed, but it is still working to some extent in sugar; there is still a combination there that keeps the price up, but whether that situation would work its way into the retail trade or not, I do not know, but still it appears to me that there is a possibility of some such thing arising.

But the thing that is still bothering me, and maybe I am dumb—I do not know, but what worries me is, where does the interbank currency come from? It is a bookkeeping transaction between the Treasury and the bank, but what is there behind it? Is the complete force of national credit going behind it? Is that the idea? I can understand it in connection with the production of goods, but after the goods have been sold and gone into consumption, it seems to me that whatever base there was for it originally is gone. I think that the idea that Mr. Goldsborough had, and maybe I am mistaken in this, but he is here and he will probably correct me if I am, is that since these automobiles that I have referred to have been moved, there is then an opportunity for the manufacturer to put 10 more in their place and put 10 more in circulation immediately, and that the base for that same credit is the 10 new automobiles. Is that right?

Mr. **Harvey**. Yes; it is the stimulation of replacement demand.

Mr. **Ford**. Is it the additional wealth that comes in as the result of that movement?

Mr. **Harvey**. Exactly, it is.

Mr. **Ford**. What possibility is there that there will be a demand for the bank to call on that money, to make up its accounts with the various depositors, to whom it has given credit? We will say that it has 100 depositors in commercial retail lines, and they have moved a lot of these goods, amounting to $500,000, in a week, on which the 15-percent discount has been given, and the banks are called on to credit on their books the amount of the discount which these dealers have been given, and the bank, in turn, demands of the Treasury that it give it credit for the amount that it has allowed to these retailers. In the transactions throughout the country, that would rapidly mount to a very large volume of money, or of credit, would it not? It might conceivably run into billions?

Mr. **Harvey**. It would run into probably about $750,000,000 a month.

Mr. **Ford**. That runs into money.

Mr. **Harvey**. We hope it would.

Mr. **Ford**. As a matter of fact, is that going to be liquidated if the banks have a call on them to make good their discount, and to protect their depositors?

Mr. **Harvey**. It comes to the same thing exactly, except that it is freed of the indebtedness, as if the Government deposited a $1,000 bond, or whatever the amount might be, to cover the discount. At the present time the Government sells the bond to the banks and takes that money and distributes it to the public somehow or other, in the relief business. Now, if the Government did that with a bond, and told the bank to apply it, instead of for relief, to honoring vouchers of the retailers on the basis of a 15-percent reduction, the situation would be precisely the same except that there would be accruing charges there which the Government would have to pay, but as far as the creation of money goes, it is practically the same proposition. As I see it, the Constitution authorizes the United States Government to issue money. It does not say anything as to whether that money is to be backed with anything or not. It is supposed to issue the money that the trade of the country needs, and to keep it regulated, and in issuing this money it is doing that without having recourse to a dual transaction with a bank which may be called borrowing, but it really is not borrowing today; it is really cooperation; but the money comes in in precisely the same way. It is a creation of credit.

Mr. **Ford**. Is the phrase in the Constitution, "to coin money and regulate the value thereof," the equivalent of a transaction of printing a dollar bill and regulating the value of it?

Mr. **Harvey**. I believe that that has been passed on by the Supreme Court. I came across it in one of the hearings, but I could not give you the name of the decision.

Mr. **Ford**. There is a Supreme Court decision to that effect?

Mr. **Harvey**. Yes.

Mr. **Ford**. And that is coining money, to print a bill?

Mr. **Harvey**. Yes. They could coin silver and gold and put it into the banks, and it would come to the same thing, and they would regulate that when they felt that the bank had built too much credit upon it.

Mr. **Ford**. I have tried to think this thing through, but I always go up against a blank wall when I come to that interbank currency. Maybe that is by reason of my past thinking on money. It may be that I am haywire, but I just cannot see it.

Mr. **Harvey**. If I might suggest it, if you could think of the Government, instead of borrowing money—and people have got so much into their heads about borrowing money that they cannot get away from it, but you make deposits in banks sometimes when you do not want to borrow money, and think of the Government making a deposit in the bank and putting the bank under the obligation, and not itself. The bank is under the obligation, when it receives that money, but it is under obligation not as a personal debt but as a fiduciary debt to the public of the United States.

Do you follow me?

Mr. **Ford**. Yes.

Mr. **Harvey**. It is just the reversed process.

Mr. **Ford**. The Government makes the bank put up that collateral for it?

Mr. **Harvey**. No; it does not. It only demands that the bank shall manage it as it manages a loan for the account of others.

Mr. **Patman**. I would like to ask the gentleman a few questions.

According to this plan, all retailers would first have to be licensed, would they not?

Mr. **Harvey**. It is advisable that they should be; yes.

Mr. **Patman**. They could not receive any benefits unless they were licensed.

Mr. **Harvey**. If they wanted to cooperate under the discount, which they certainly would want to do——

Mr. **Patman**. In other words, if they are to receive the benefit of this law, they must be a licensed retailer; isn't that right?

Mr. **Harvey**. Yes.

Mr. **Patman**. The census reports that there are 1,653,000 retailers. In addition to that, this law includes dwellings. I presume that that would include real-estate operators, would it not?

Mr. **Harvey**. I am not sure how the law is worded, but the idea is to cover rents.

Mr. **Patman**. The bill covers goods, including dwellings and services.

Mr. **Harvey**. Including rents on dwellings.

Mr. **Patman**. It says here:

> The term "retailer" means any seller of goods, including dwellings, and services, to ultimate consumers who are natural persons.

And then it goes ahead and defines the term "services" to mean—

> passenger transportation, distribution to homes of gas and electricity for domestic purposes, rental of homes, hospitalization, schools, and theaters.

In other words, it includes retailers, it includes dwellings, which, of course, would be a home, and really it should include a home, I presume—a home is just as necessary as anything else, if you are going to help the ultimate consumer—and it would include all of the real-estate operators, and there must be several hundred thousand real-estate operators, including rental offices, are there not?

Mr. **Harvey**. Quite.

Mr. **Patman**. And then, all engaged in passenger transportation, like the railroad companies and the bus companies and the taxicabs—they would be licensed under this bill—and then it would include the hospitals of the country; and there must be tens of thousands of hospitals, are there not?

Mr. **Harvey**. Yes.

Mr. **Patman**. And it includes all the schools and all the theaters. Now, that would require a lot of licensing, would it not?

Mr. **Harvey**. I do not know that it would require any more licensing. I think that the licensing would be very much the same proposition, don't you, that we had under the N. R. A.?

Mr. **Patman**. Well, yes; but it was not effective under the N. R. A. They had no power there. They had a good purpose, like this is a wonderful purpose that is expressed in here by Mr. Goldsborough, and I commend the purpose that is behind Mr. Goldsborough in trying to get a bill through, but it occurs to me that this is top-heavy with details and mechanics and opening of the floodgates for fraud. That is what I am afraid of. For instance, under this bill, if I have an automobile to sell, I cannot sell it to you and give you a 15-percent discount, because I am not a retailer, but I can sell it to one of these licensed retailers, and he could sell it to you, and you would get the 15-percent discount. Of course, that would force all business through the bottle necks of retailers and those who have licenses under this law; and as to whether or not that would be a good thing to do, I do not know.

Then, for instance, take a small store. You go into that store to make a purchase, and whether it is a package of Chesterfields, or an automobile tire, or an automobile, you certainly would have to make some record of that, would you not? In other words, the retailer must say to you, "Mr. Harvey, I have to carry this to my local bank to get the 15 percent, and I have to have some evidence that you are buying this not for resale, but for your own personal use, and the only way that I can do that is for you to sign this statement and certify to these things," and then you would certify to that on every purchase that you make. That is going to require a lot of book work and extra help on the part of these retailers, is it not, Mr. Harvey?

Mr. **Harvey**. Well, I have got to look at this thing from the point of view of the business experience that I have had.

Mr. **Patman**. Don't you think that you ought to look at it from that standpoint?

Mr. **Harvey**. I say, I have to look at this thing from the point of view of the business experience that I have had, and I know something about the details involved in the bookkeeping, for instance, of a telephone company, or of the American Telephone & Telegraph Co., or of the General Foods Co., and of smaller businesses, and personally while I do not think that I could demonstrate it here before this committee, I feel sure that it would be quite possible to work out these details if the policy of the bill is considered to be one that is worthy of attention, and if it ever becomes law, the ability of the human being to organize things of this sort has been so thoroughly demonstrated—I think that we Americans have been a long way ahead of the world in doing it, and I do not think that there is any bridge that cannot be crossed. It would take work; it would take what my engineer friends like to call the collective brain to do it, but I see no serious obstacle, and as far as the complication in connection with the sale of goods which might be resold is concerned, I would like to call attention to this, in connection with small sales for personal use and not for resale, that, in connection with the sale of one pair of shoes or one refrigerator, the retailers know their customers pretty well, and they know that a man does not buy a pair of shoes to go out and sell them at a higher price to the man next door, or that that man might go out and buy them——

Mr. PATMAN. I understand that the retailer would probably know it——

Mr. HARVEY. May I finish the trend of thought?

Mr. PATMAN. It is really not what I am asking you about.

Mr. HARVEY. Therefore the smaller transactions I do not think offer a serious problem. Furthermore, the development of the business machine, the cash register, and that sort of thing, has been so tremendous that I think that a great many of the transactions involved would be covered by them—in other words, where it is said in the bill that a voucher is necessary, the machines could do that; the machines are the most capable voucher makers, and they are even capable, when you sign large bulks of corporate bonds, of enabling you to use one pen with, I think 20 extra pens on that machine, so that you sign 20 signatures at the same time.

That is merely an illustration of what the machines can do, and I think that it is a very simple thing to use a cash register or other such equipment to keep a record which could be used by the retailer as his voucher, without anyone signing anything.

Mr. PATMAN. Without the customer signing anything?

Mr. HARVEY. Without the customer signing anything.

Mr. PATMAN. Do you mean to say that you would force on these little retailers the necessity of going to the expense and trouble of buying these expensive machines or of keeping the help there to do that book work, one or the other? It would have to be one or the other?

Mr. HARVEY. Well, of course, I am looking at this thing from the standpoint of 40 billion dollars of turn-over of business——

Mr. PATMAN. I know that you are, Mr. Harvey, but——

Mr. HARVEY (continuing). And I am not paying so much attention at the present time to that perhaps 500 million turn-over of these smaller retailers, because I think that that is a secondary thing, a bridge that we can cross later.

Mr. PATMAN. But the first bridge that we have to cross is to put this measure into practical operation, to put it to work, and I believe that there is about $30,000,000,000 worth of business that would be done this way.

Mr. HARVEY. I think between 30 and 40 billion; it would be nearer 40 billion.

Mr. PATMAN. Now, 15 percent of that is $6,000,000,000, is it not?

Mr. HARVEY. Yes.

Mr. PATMAN. And $6,000,000,000 of this interbank currency would be issued. What is behind that currency? Is there any gold behind it?

Mr. HARVEY. If you wish to put gold behind it, there is no reason in the world why it should not be put upon that basis that I can see, speaking for myself. I cannot speak for Mr. Goldsborough.

Mr. PATMAN. What is behind it under this bill?

Mr. HARVEY. Under this bill nothing is behind it, as I understand it, except a flow of business upon the replacement demand.

Mr. PATMAN. Of course, the volume of business passes on; that is something behind us rather than in front of us.

Mr. HARVEY. Yes.

Mr. PATMAN. And in 2 years we would have $12,000,000,000 in interbank currency. Who would pay that?

Mr. HARVEY. Personally, I do not think——

Mr. PATMAN. We will presume that it runs 2 years at 15 percent for the purpose of this discussion, and we would have 12 billions of interbank currency. Who would pay that money?

Mr. HARVEY. Nobody.

Mr. PATMAN. It is rather strange money, is it not?

Mr. HARVEY. Not at all. If anybody wanted cash out of the bank, would you not do the same way now?

Mr. PATMAN. But you know that there is a pay day that is coming, and somebody has to be the paymaster. Who will be the paymaster?

Mr. HARVEY. There will be no increase in the amount of the currency in circulation, or no reduction of the currency in circulation.

Mr. PATMAN. There will be no paymaster and no pay day?

Mr. HARVEY. Why not?

Mr. PATMAN. I cannot find out who the paymaster is going to be.

Mr. HARVEY. I do not quite understand how you mean.

Mr. PATMAN. I mean this: We will say that this goes on for 2 years, and that there is 12 billion of interbank currency out. Who is obligated to pay it?

Mr. HARVEY. Whom is it owed to? I would like to ask that question.

Mr. PATMAN. It is owed to the banks that had the money, and then cashed it to the retailers. They had the money in their vaults, and one bank over here in Pennsylvania will say, "I want my money, and I need it," and they will say, "We will give you credit." And the bank will say, "We do not want credit. We want the money, and we need the money."

Who will pay it?

Mr. HARVEY. In other words, if the bank needs the money, because it is being squeezed?

Mr. PATMAN. Maybe they are not being squeezed. Maybe they want it for no reason at all. They have a right to demand it.

Mr. HARVEY. I do not know. I have been in the banking business, and I have not found banks wanting things for no reason at all.

Mr. PATMAN. Suppose that they decide that the banking business is such that they cannot make any money, and they want to pay off everybody and get out of the business.

Mr. HARVEY. Then they would call their loans first, and if they were managing their business properly, when they called all of their loans they would have a surplus reserve sufficient to return that currency to the Government. It would pay back its deposits to the Government and the public in exactly the same way; it would liquidate the loans and pay back the deposits, including the interbank currency to the Government.

Mr. **Patman**. But the Government owes the banks, not the banks the Government.

Mr. **Harvey**. No, sir; pardon me. The Government has made a deposit in the bank, just as you might make a deposit in the bank, so that that bank owes the Government.

Mr. **Patman**. The bank owes the Government?

Mr. **Harvey**. Yes, sir. That is the key to the whole problem.

Mr. **Patman**. Do you mean to say now that when I go in and buy this $100 refrigerator, and I sign up that I have bought it for home use, and so forth, and the retailer takes that to the bank, and the bank gives the retailer credit, just the same as if it was money, and then the Government issues its interbank currency for $15, that means that the bank owes the Government that $15?

Mr. **Harvey**. That means that the bank has got a deposit from the Government of $15.

Mr. **Patman**. That the bank has got a deposit from the Government of $15?

Mr. **Harvey**. Which the bank is responsible for as fiduciary, as an agent.

Mr. **Patman**. Just as a trustee?

Mr. **Harvey**. Yes.

Mr. **Patman**. I know, but the bank put out $100 in hard cash for that.

Mr. **Harvey**. Pardon me; I must differ with you there, because the bank did not even put up the $15 in hard cash which would be the 15 percent discount. What the bank put up was a write-up on its own books, and nothing more.

Mr. **Patman**. The bank is compensated for that $15 by the Government delivering to the bank $15 in interbank currency, is it not?

Mr. **Harvey**. By the Government depositing $15.

Mr. **Patman**. I just cannot follow you all the way, Mr. Harvey. Maybe I just do not understand these things like you do, but I would just like to know this: Suppose that they say to Uncle Sam, "I do not want that $15 in interbank currency. I want my money right back." Who will pay that?

Mr. **Harvey**. The Government would say, "You have issued credit against it; you now call the credit in." Otherwise, you see, there would not be any cooperation to provide the flow of money. You are suggesting that the banking system as a whole——

Mr. **Patman**. I do not understand——

Mr. **Harvey** (continuing). Not an individual bank, because it can do anything, but that the banking system as a whole shall not conduct its business to circulate money.

Mr. **Patman**. I cannot understand why it is that you can put 6 billion dollars out in 1 year, which is 15 percent of 40 billion, of this interbank currency, with nobody behind it, with nobody guaranteeing it, with no pay day, no paymaster. I just cannot understand that part of this bill, Mr. Harvey.

Mr. **Harvey**. The only way that I can answer that is to ask you whether the same thing did not exist in 1933, when we had 45 billion of deposits in the banks and the banks did not have the money to repay it. That is the whole principle of modern banking, and this bill is built upon the same principle.

Mr. **Patman**. Another thing that bothers me is that it just opens the door to fraud; that if you are not requiring the customer to sign a thing, then all that the retailer has to do is just to certify that he has sold John Smih $100 worth of goods in order to collect $15 from his local bank, and then if the inspector comes in and asks, "Who is John Smith?" he may get the answer, "I do not know him; he just came through here and needed a pair of shoes and a refrigerator and things like that."

I am not convinced that that is not enough for me.

Mr. **Harvey**. Permit me to answer that. The use of business recording machines is part of the mechanism that could be used.

Mr. **Patman**. But all of the smaller retailers could not buy that machine.

Mr. **Harvey**. And I think it is much simpler than you realize. I do not think that the opportunity for chiseling is anything like you realize, for the reason that no retailer can get a credit without a cash deposit. In other words, if he sells $100 worth of goods for $85 he cannot get his $15 discount until he deposits his $85. Now, if a man wants to chisel, and he has to go to some friend and say, "Give me a check for $100 and I will put it in the bank and I will get $15 additional credit, and tomorrow I will give you your check back and I will be in $15, he will have no vouchers for the goods; he has to go through a complete fraudulent issue of sales slips with the man from whom he gets the money in order to get $15 by committing a crime involving $100 by falsifying the accounts and collusion with another man to do it.

Mr. **Patman**. But suppose that he does it with himself, that John Smith is a fictitious person, he does not exist at all, and as he does not have to sign a receipt or a voucher there is no way to check up. You have to read the retailer's mind or apply a lie detector to find out if he is telling the truth, and don't you think that the Government would be put in a bad position in seeking evidence in cases like that, with 1,653,000 retailers and 400,000 or 500,000 real-estate operators and rent dealers, and hospitals and schools and theaters all over the country? Don't you think that it would open the floodgates to the possibility of the fraud that I have referred to?

Mr. **Harvey**. I think that the Government would be precisely in the same position as it is with one million and a half of income-tax payers.

Mr. **Patman**. I know; but there is a record there; you see, you have to put down everything and sign your name and swear to it before a notary public, and if you require that in that case it will take all of the unemployed to carry out the enforcement of this bill.

Mr. **Harvey**. Of course, I cannot agree with you, because I happen to be a businessman, and I feel that it can be done without such a great amount of difficulty.

Mr. **McKeough**. May I ask a question that was developed in the questions of Mr. Patman?

On page 15 of this proposed act, paragraph (h) reads as follows:

> In the event of the banks having to face an emergency demand for currency by depositors beyond their ability to meet without dangerous forced liquida-

tion of their quick assets, said banks may apply to the Secretary of the Treasury for permission to convert interbank currency into national currency notes by presenting the former for exchange.

In the event there should be a tightening up of economic activities, would that authorize the banks to go to the Treasury and exchange interbank currency for national currency? In the event that that developed, and assuming that we went through a forced liquidation such as almost every large country in the world has passed through in the last 6 or 7 years, probably 100 percent of this outstanding interbank currency that Mr. Patman referred to as being issued over a period of 2 years would be exchanged for national currency, and with 12 billion of national currency outstanding in exchange for the interbank currency we would have the very thing that everybody is talking about in the country today, which is inflation, of a degree that would be ruinous. I am very frank to confess openly that this particular proposed enactment is so phrased with language that opens up possibilities of new experiences that we are liable to find ourselves in a chaotic condition in the application of its provisions. Certainly it is obvious that with 1,600,000 retailers, excluding those in the hospitals, schools, and other activities that Mr. Patman has touched upon, that we would have to have an army policing the provisions of this particular activity, and if we are speaking of delegation of power as a very undesirable thing in this Nation, this, in my judgment, delegates more power to those that are assigned the gigantic task of enforcing its provisions than has ever been delegated by any enactment of Congress in the history of the Nation.

I think that there may be some value in the discussions that will come out in the consideration of this measure, but I am very fearful that the things that you complain about in your prepared statement would be made worse by the enactment of this bill. Among other things, you touched upon the staggering indebtedness not only of the National Government but of the various subdivisions of local government, and particularly of corporate activities in the industrial world. You complained about that debt at its present high level and the apparent inability of this Nation of 130,000,000 people by their activities to create sufficient wealth to care for the payment of that staggering funded debt, and you pointed out in your statement, as I understood it, that it will be almost impossible to amortize it. You spoke of the wealth stepping up from 3 to 4 percent a year and the debt structure from 5 to 8 percent. It is obvious that if we continue that governmental fiscal policy, and if we have no control of the securities put out by the corporate activities of the Nation, except as provided for in the securities and exchange law, that we will continue to have a rapidly mounting debt structure, at a speed that will only require a few years until there is a collapse; and, if that is the problem, I am wondering whether or not we could give it a simpler treatment than this bill provides?

Mr. HARVEY. I am entirely open-minded on that. I have been looking for a simpler method, but I have been unable to find one.

Mr. MCKEOUGH. Unhappily, it seems to me that the world, and our Nation among the nations of the world, has been seriously handicapped by its inability to properly control the monetary activities of our Government. It is quite obvious from the history of the world that some particular group, some influence, some very powerful influence that is usually referred to for the purpose of an abstract identification as the international bankers, has that power. Does it not seem rather strange that a nation that you so eloquently eulogized in its initiative and ability to meet these problems that Mr. Patman developed in his questions on this bill is so impotent, and that the people, speaking of them in a crude, abstract way, reflecting their power through government, are so completely defeated in their efforts to bring about a cure? What the cure might be, I do not know. I have spent more than a quarter of a century trying to find it out, but I am as far away from the answer today as I was, I think, the first day I determined that I would try to find out. I am convinced that there is such a powerful influence, or group, or clique, that regulates th monetary situation not only of our Nation but the world, and it is not lodged in government——

Mr. Harvey (interposing). It is not the Government.

Mr. McKeough. No; it is foreign to government. I am convinced in my own mind that governments are controlled by that particular group, and I am perfectly willing to concede that this Government is so controlled, but I think that this administration is at least making an attack on the causes of a depression, which, in other words, is the banking structure of the world.

Now, I would like to find somebody in government, first, with the ability; second, with the courage; and, third, with the patriotism to attack the problem; and I want at this time to pay due respect to my colleague, Mr. Goldsborough, of Maryland, who has introduced this bill. I think that it is at least an opening wedge that might, by reason of its study, bring about the solution that I am confident the great majority of the people of this Nation would like to have brought about. I do not believe, however, by reason of the difficulties that surround the application of this particular proposed enactment, that the answer is there. I may be wrong, but I do not believe that we have the answer in this bill, and I merely wanted to point out for the record that particular phase that you brought out in your statement, of the unhealthy relation of increased wealth to the constantly mounting funded indebtedness or long-term debt, not only of the National Government but of subdivisions of local governments, and particularly in the corporate field.

Mr. Patman. I want to ask one other question, Mr. Chairman, and I will be through. The objections that I have pointed out to Mr. Harvey may be considered minor as compared to the one that I consider major, and that is that this bill would force lower prices if enacted into law. I have read the books of Maj. C. H. Douglas and I have studied his proposals. At one time I had the privilege and the honor and the pleasure, with my good friends Steagall, Goldsborough, and others, to hear Major Douglas, and Major Douglas says that he is in favor of a discount like this for the reason that it will force lower prices. He says that in his books. If for no other reason, I think that I would be compelled to oppose it for that particular reason, and one reason that it will force lower prices is this:

You take eggs. That is a commodity that is sold in every community in this Nation by the farmers themselves. If the farmer carries his eggs to town to sell them to you, you cannot buy them from him, because he cannot give you a 15-percent discount. He has not got his license. You would have to buy them from the retailer. Therefore, he would be forced to sell his eggs at a 15-percent discount in order to get your business, and that would happen in all other commodities, and anything that you could mention that is sold in the retail trade. It would force retail prices down, and Major Douglas admits that it would force lower prices to that extent, and he thinks that it would be a helpful thing. Possibly he is right, but I just do not agree with him.

Then, for instance, under this law a corporation cannot buy automobiles and get the 15-percent discount; and if I owned a corporation, and I wanted to buy an automobile for my own use, I could get it, but if I wanted to pass it on to the corporation at full price, I guess it would be all right; that is just a minor violation, but this bill opens up the gates by letting individuals purchase things and pass them on to those not entitled to the benefits of this law and to receive a split if they want to do it. Those are just some of the little things that could happen.

But the main thing that this would force would be a reduction of prices, to the amount of the discount. Major Douglas admits it, and he says it is a good thing. But I take issue with him and others having the same view, because I think that it would be a bad thing.

Don't you think that lower prices would be a bad thing rather than a good thing?

Mr. Harvey. To begin with, you have asked me three questions, which I can answer separately. I had better take Major Douglas first.

I would like to say that I disagree with a number of Major Douglas' deductions altogether. I have given them some study. In the earlier part of my studies along these lines, I did pay a good deal of attention to Major Douglas, but I found, in my opinion, that his theory on money was entirely wrong, and also that his A plus B theorem gave me a pain. But I do not want to discredit Major Douglas in any way, because I think that he is an able man and he has made some very interesting developments in connection with the economics of modern industry, but his contentions are wrong. One of his theories on money is that you can put any quantity of money into the world that you want to, provided that you regulate the prices of retail goods, and it won't make any difference. I do not agree with that, but——

Mr. Patman (interposing). But this particular——

Mr. Harvey (continuing). But under Major Douglas' theory and method of approach on money, I think that the tendency would be for the wholesale price level to rise——

Mr. Patman (interposing). You think——

Mr. Harvey (continuing). Under H. R. 7188, the tendency would be to carry on a similar rise to the one that we have had recently, because the effort in this case is not to expand the money supply to an unlimited extent, which is Douglas' theory, but to limit the money supply so that money and goods flow side by side in equal quantities. Money and goods should be practically the same, and the volume of money and goods——

The Chairman (interposing). Gentlemen——

Mr. Patman. I am through, Mr. Chairman.

The **Chairman**. Does anybody else desire to interrogate Mr. Harvey further?

Mr. **Goldsborough**. Can you be here tomorrow?

Mr. **Harvey**. Yes, sir.

The **Chairman**. Suppose that we adjourn until tomorrow.

Mr. **Luce**. I have one or two questions.

The **Chairman**. Would it be all right with you to adjourn until tomorrow?

Mr. **Luce**. I can get through with him by merely asking him two questions.

The **Chairman**. Very well.

Mr. **Luce**. In one part of Mr. Patman's interrogation of you, he brought up a point that I will carry just one step further. Suppose that there is a serious defalcation in a national bank in my town, and a receiver is appointed, and he finds $100,000 of this interbank currency. Isn't that an asset?

Mr. **Harvey**. That is an asset; yes.

Mr. **Luce**. Why?

Mr. **Harvey**. Because the bill provides that the bank may liquidate that by applying to the Secretary of the Treasury for currency. The national currency will then be charged to the liquidator of that bank, and the national currency would be returned to the Treasury as the bank was liquidated, just in the manner that is done today.

Mr. **Luce**. Then is it the fact that the total outstanding amount of interbank currency would be a debt of the United States?

Mr. **Harvey**. No. That is what I have been trying to point out, that it is not a debt of the United States at all to the banking system. It is an issue of credit to the people of the United States to maintain a sufficient volume of money in circulation——

Mr. **Luce**. You do not catch my point. If this is an asset of the bank, then it is a debit of somebody else. To whom is that a debit?

Mr. **Harvey**. Well, I think I tried to state that the currency was an asset of the United States Government.

Mr. **Luce**. That is not the question. I think that you ought to be able to answer whose debit is that asset.

Mr. **Harvey**. That asset is a debit of the bank.

Mr. **Luce**. Whose debit?

Mr. **Harvey**. It is a debt of the bank.

Mr. **Luce**. But you just told me that the receiver would call it an asset. When he comes to liquidate the bank, he has to determine what are the assets.

Mr. **Harvey**. Well, sir, it is just as much an asset as is an insurance policy for deposits; it has precisely the same relation to the assets of the bank.

Mr. **Luce**. You are confusing me, instead of helping me.

Mr. **Harvey**. I am very sorry. It is because I do not understand.

Mr. **Luce**. If that money is an asset of the bank, it means that somebody else owes that money.

Mr. **Harvey**. What I say is that it is not an asset of the bank. In other words, the bank does not own it. The Government owns it.

Mr. **Luce**. Then the bank is $100,000 out of pocket.

Mr. **Harvey**. The bank has deposits against it.

Mr. **Luce**. Well, I am sorry. I cannot understand you.

Mr. Harvey. A bank has the deposits against it, that gave rise to it.

Mr. Luce. When a receiver comes into a bank, he finds a piece of paper of $100,000 of interbank currency. As I understood you, he puts that down as an asset of the bank. Now, I think that you are making it a debit of the bank.

Mr. Harvey. I am very anxious to get you straight, because you have raised a very interesting point, and I think that it can be cleared up, but we are looking at the thing in a rather different manner, and——

Mr. Luce. I do not think that it takes a long answer. I think somebody can tell me who is to pay the receiver if that is an asset of the bank.

Mr. Harvey. I would like to go back to the illustration that I used in answer to one of Mr. Ford's questions.

Mr. Luce. But we have not time. I am sorry.

Mr. Harvey. I hope that you will give me the opportunity of discussing this thing privately with you, or in committee. I should very much like to get thinking along your question.

Mr. Luce. You ought to know who owes the money.

Mr. Harvey. Nominally, the bank would owe it.

Mr. Luce. The bank would owe it?

Mr. Harvey. Yes.

Mr. Luce. A bank cannot owe an asset. You said that it was an asset.

Mr. Harvey. We will have to begin, I think, a little further back.

Mr. Luce. I do not want a long discussion, but an answer.

Mr. Harvey. May I ask a question that will answer it? Supposing that you went to a bank with a $100 bill and deposited that $100 bill, and supposing the next day the bank closed its doors. Would that $100 bill be an asset of the bank's or would it be a liability of the bank's?

Mr. Luce. You know much more about that than I do.

Mr. Harvey. It would be both an asset and a liability, because your deposit would be a liability, but the $100 bill would be an asset.

Mr. Luce. If it is an asset, you have not told us who will pay it.

Mr. Goldsborough. It may be that the witness cannot answer that yes or no. It may be that it requires an explanation, and that is what the witness says.

Mr. Luce. I do not want to embarrass him, but I cannot think this thing through until I know who is going to pay the receiver.

Mr. Goldsborough. In my opinion, if we will listen to him about 5 minutes, we will find out about that, if we do not interrupt him.

Mr. Luce. I am doing it solely because of the chairman's desire to adjourn.

The **Chairman.** We will stay long enough for him to answer it.

Mr. Luce. If your explanation comes to the point as to who owns that money, I should be very glad to hear it.

Mr. Harvey. My statement is very distinctly that the Government owns the money. The Government has made a deposit in the bank, and the Government owns that money. If the bank gets into trouble, and the Government says, "We will defer our claim for a deposit, and will allow you the currency necessary to take care of your liability against this deposit," that is the Government's business, is it not?

Mr. **Luce**. Now, I understand it is the Government that owes that money?

Mr. **Harvey**. Yes. The Government will honor that, just as it will honor an insurance policy against deposits if the bank gets into trouble. It is a supplemental insurance. In other words——

Mr. **Luce** (interposing). I appreciate that, but I have not yet found out if the Government owes the money.

Mr. **Harvey**. No, sir; the Government—I might come back to the illustration again where, if you put $100 into a bank, do you owe the bank $100?

Mr. **Luce**. If the bank has a piece of paper, it is either a proof of title to receive or proof of duty to give. Brought down to its simplest terms, it is either an asset or a debit.

Mr. **Harvey**. Of course, a deposit against which there is no loan——

Mr. **Luce** (interposing). But you are telling me how it will be met. I am not interested in that. You are talking to me about balancing obligations. You are telling me something outside of what I am asking you. What I am trying to find out is this—that if the interbank currency is an asset of the bank, then the total outstanding interbank currency is a debit of somebody else. Whether there is security for it is not my instant question. I am simply trying to find out whether this proposal involves a recognition by the Government that it owes to the banks of the country a total amount of money equal to that of all of the outstanding interbank currency.

That is all, Mr. Chairman.

Mr. **Crawford**. Will the witness be here tomorrow?

The **Chairman**. If there are any more questions, he said that he would be with us tomorrow.

Mr. **Goldsborough**. Mr. Harvey, I think the explanation is simple, and I wish that you would work it out between now and tomorrow. Can you be here tomorrow, Mr. Luce?

Mr. **Luce**. I do not know.

Mr. **Goldsborough**. I really think that there is a clear misunderstanding between Mr. Harvey and you as to just what your question is and what his answer relates to, and I think that he can clarify it in a few minutes if he is given that opportunity.

The **Chairman**. Very well; we will adjourn now until tomorrow morning at 10:30.

(Thereupon, at 12:20 p. m., an adjournment was taken until Thursday morning, July 22, 1937, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, JULY 22, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members present: Messrs. Goldsborough, Reilly, Hancock, Williams, Spence, Ford, Brown, Patman, McKeough, Transue, Luce, and Crawford.

The **Chairman**. All right, gentlemen; come to order please.

Mr. Harvey, you may resume your statement. I believe that some of the members of the committee desired to interrogate you further. Were you through, Mr. Luce?

Mr. **Luce**. I understand that Mr. Harvey will answer the questions that I asked him yesterday.

STATEMENT OF EDWARD F. HARVEY, OF GWYNEDD VALLEY, PA.—Resumed

Mr. **Harvey**. Mr. Chairman and members of the committee, I just have a short answer which I have tried to prepare to Mr. Luce's question. I also have an answer which I would like to present to Mr. Patman's question, because there was not time yesterday to complete that answer. There were three questions that he asked, and I tried to prepare an answer to them. So I will first try to answer Mr. Luce's question.

The interbank currency is deposited in the banks. As such it is credited to the Government on the books of the banks. The Government owns it. Deposits arising from the discount vouchers are credited to the individual accounts of those presenting them, and are charged to the interbank currency account. This account would therefore be in balance and should be so at all times.

There is no debit and credit liability there. That is a balanced account. The liability, whatever it may be, is between the Government, in its effort to maintain a balanced currency, and the public which needs that currency.

That is the answer as I see it. But it is really not money, in a sense. It is not money such as is created when a bank goes to the Comptroller of the Currency and gets currency and pays it out in the form of a demand check or cash check for a customer. It is not that type of currency at all. It is an authority, really, a warrant for issuing money to the bank, if you understand. Therefore it does not come under the debit idea at all. It is really a warrant for issuing money. The banks have a blanket warrant at the present time for issuing money or fractional reserves. They will issue money on fractional reserves against their existing deposits. The two tend to balance each other, so that that money goes out, and that is a blanket authority from the Government, over which the Government has practically no control at all. The bank can inflate its credit without any control of the Government, unless the Government, through the powers of the Federal Reserve Bank, comes in and sells Government bonds, which will reduce the ability of the banks to expand credit.

That is the mechanism at the present time, but it makes for a very fluctuating currency. The currency is up one year and down the next, and that fluctuating currency has a very serious effect upon the price level. In fact, that fluctuating currency—and I am speaking now of currency and bank checks and things of that sort as well as national currency—becomes a very fluctuating item. It varied in 1929 and 1932 some 15 billion dollars or more, which took money completely out of circulation.

Now, this question, Mr. Chairman, instead of being a debit and credit between the banks and the Government, is an authority, a specific authority to issue the same type of money that the bank now has a blanket authority from the Government to issue. Do I make myself plain? It is a supplementary authority. The bill does not remove the blanket authority, but it gives a supplementary authority, which gives the monetary authority, whatever it may be, the Federal Reserve Board or whatever may finally be decided upon, the necessary control to reduce the volume of currency and credit in circulation, without disturbing the present banking system at all. It simply calls its loans in exactly the same way that the bank calls its loans at the present time if there appears to be an inflationary condition, or the Government can again force, as I say, that reduction by selling Government bonds to the bank and calling in their surplus reserves in that way.

Do I make myself clear, Mr. Luce?

Mr. **Luce**. Yes, on the point that you have discussed, but that is not the point that I was driving at. Our minds have not yet met on that point.

Referring again to my illustration, take the bank that has gone into receivership, and a receiver finds in the vault $100,000 in interbank currency. What I want to know is whether he is going to be able to get $100,000 to pay over to the creditors of the bank.

Mr. **Harvey**. Under this bill, as far as the interbank currency goes, he may do that. He can apply to the Secretary of the Treasury or to the Comptroller of the Currency, or whoever it may, to get $100,000 in national currency, or some other form of bank credit, to pay out the deposits. On the other hand——

Mr. **Luce**. That is not my question.

Mr. **Harvey**. May I finish that? Then the Government becomes a general creditor, practically, upon the assets of the bank, and will be reimbursed as far as its own credit is concerned in the ultimate settlement of the bank's affairs. In other words, if the bank pays off 30 cents on the dollar or 50 cents on the dollar, and if the latter, 50 cents on the dollar will be returned to the Government and the

Government will be in position to take its share of the loss, just as it will do when it has to pay up on these insured deposits.

Mr. **Luce.** That I do not understand at all. I had supposed, when we recognized that $100,000 as an asset of the bank——

Mr. **Harvey.** But it is not an asset of the bank as far as its own affairs go. It is a guaranty to the public, by the Government, that the money that the bank has been handling for the Government and for the public is good to the extent of $100,000.

Mr. **Luce.** Suppose that the bank is settling up on the basis of 30 cents on the dollar. Do I understand you to say that this $100,000 in interbank currency will only be worth $30,000?

Mr. **Harvey.** It would be worth under those circumstances only $30,000—that is, it would be worth the full $100,000, but, as far as the Government is concerned, the bank having a reversional liability to the Government, it would be only worth $30,000.

Mr. **Luce.** Then you put it on a plane quite different from any other type of money?

Mr. **Harvey.** From any other type of money.

Mr. **Goldsborough.** It is not money at all.

Mr. **Harvey.** It is not money at all any more then the insurance policy covering the deposits is money. It is not money; it is a guaranty really.

Mr. **Luce.** But the bank acquired that $100,000 for the purpose of paying it over to somebody else, did it not?

Mr. **Harvey.** You will pardon me, but the bank has no right to claim that money.

Mr. **Luce.** Just take my statement. How did the bank acquire that money? Did it acquire the money as the result of paying money out?

Mr. **Harvey.** It acquired it as the result of the Government paying out money, and then it paid that money out.

May I just sketch this? Perhaps this will answer the question.

The transaction is fiduciary as far as the banks are concerned. The banks occupy the same position as the trustee of an estate who receives cash and securities. He is not in debt, except insofar as his responsibility for the management of the funds is concerned.

Now, the bank is placed by the Government in the position of a trustee of an estate, in exactly the same way that I have been a trustee of a good many estates, and I have never been held as a debtor to the estate. I have been responsible, but my responsibility to the estate was only for efficient and honest management.

Mr. **Luce.** Then the bank never owned the interbank currency?

Mr. **Harvey.** No; the bank never owned the interbank currency in that sense.

Mr. **Luce.** And it is not an asset of the bank?

Mr. **Harvey.** It is not an asset of the bank. It is an asset to the point of the currency and the deposits that it has given rise to. In other words, the bank has no excess liability or decreased liability on account of it. The liability and the asset value balance, and must be kept balanced all the time. So that there is no liability of the bank, and no liability of the Government to the bank, but, as I say, it is not money so much as it is a warrant to the banks to issue money in specific amounts, to supplement the warrant that the banks have, to issue money to any extent within their reserve ratio.

Mr. **Luce**. Then the use of the word "currency" to designate those issues is a misnomer?

Mr. **Harvey**. Well, that is a subject for debate. I have no personal feeling that the name is either the best or a misnomer. It is a question which can be decided by perhaps better minds than mine. The word, I think, was used in order to clarify the bookkeeping relationship between the banks, the public, and the Government.

Mr. **Luce**. Would you expect the bank, as a trustee, to keep an independent account of this money, and not to intermix it with its own funds?

Mr. **Harvey**. Of course, the circulating deposits would get intermixed. They would circulate throughout the banking system, but in circulating the currency in harmony with those, they would have to keep a general account, which would be a simple account, I think. I have worked that out. I do not have a copy of it here, but I have worked out that bookkeeping arrangement, and I think that it is very simple, and I should be very glad to send you a copy of it or make it available for the record.

Mr. **Goldsborough**. I suggest that it be made a part of the record.

The **Chairman**. Without objection, that may be done. You will give us a copy of it for the record?

Mr. **Harvey**. I do not have it here, but I will send it to the recording officer.

Mr. **Goldsborough**. Send it to the clerk of the committee.

Mr. **Luce**. What I have been driving at all through this is to find out whether, in what is called the statement of the public debt of the United States, this interbank currency would be entered as a contingent liability.

Mr. **Harvey**. I think not, no.

Mr. **Luce**. Then the Government assumes no responsibility for the ultimate redemption of this currency?

Mr. **Harvey**. The Government does assume, under this bill, the responsibility of maintaining the value of the whole of the currency in circulation, which is 6½ billion dollars at the present time, but it may use those credit warrants which have been designated as interbank currency for the purpose of maintaining that status.

Mr. **Luce**. But it cannot maintain that status if, when a bank fails, $100,000 is cut down to $30,000.

Mr. **Harvey**. The public does not lose that. The value of the national currency is not affected.

Mr. **Luce**. But I am talking about whether this is a contingent liability of the Government.

Mr. **Harvey**. It would be to that extent; yes. In other words, the Government could lose the face value there if a bank was insolvent.

Mr. **Luce**. Then, inasmuch as 10 billion dollars is to be issued, there would have to be inserted in this table the item "contingent liabilities on account of interbank currency, 10 billion dollars"?

Mr. **Harvey**. No; I do not thing so; because you cannot estimate what the contingent liability is.

Mr. **Luce**. You cannot estimate what it is in connection with these alphabetical agencies. Something like 60,000 houses will be foreclosed on properties covered by the Home Owners' Loan Corporation. For instance, I notice that under "Other obligations" are listed Federal Reserve notes, and they do not dare to put a figure against them; there is no indication of what it is.

Mr. Harvey. I think that the same thing would apply to the currency. The Federal Reserve notes would probably be pretty similar to the interbank currency notes. They would probably be the same, except that the Federal Reserve notes can be used when deposited in the bank to expand reserves and permit a very much greater expansion of credit than the interbank currency notes can. The expansion of credit on the interbank currency notes is limited. The expansion of credit on the Federal Reserve notes that go into a bank is not limited.

That is a very vital difference between the two.

Mr. Ford. Will you permit one question there, Mr. Luce?

Mr. Luce. Go ahead.

Mr. Ford. Suppose that the depositor deposits $45,000, and he has $15,000 interbank currency credit on that, which we will say is 15 percent on a $60,000 deposit. When the bank enters that as a $60,000 deposit, do they put up separate reserves against the whole $60,000, or against the $45,000?

Mr. Harvey. It sets up its own reserves against the $45,000.

Mr. Ford. Not against the $60,000?

Mr. Harvey. No; because it holds 100 percent of the interbank currency against the balance.

Mr. Ford. It does not affect the bank's reserves?

Mr. Harvey. It does not affect the bank's reserves or the percentage of reserves. It is an attempt to keep that separate from the bank's general business.

Mr. Luce. Is it fair to say that with this entry that will be made, of 10 billion dollars contingent liability, the currency of the country will have expanded 10 billion dollars?

Mr. Harvey. Yes; the currency of the country would have expanded 10 billion dollars.

Mr. Goldsborough. Mr. Harvey, excuse me a minute. You do not mean that it would be expanded immediately upon that entry in the books?

Mr. Harvey. No.

Mr. Goldsborough. It would be expanded when the goods that went into consumption matched that currency dollar for dollar?

Mr. Harvey. That is correct.

Mr. Luce. That is very true; but we have a contingent liability of 10 billion dollars, and the significance to me would be that we are that much more in the red.

Mr. Harvey. I cannot think along with you, because a contingent liability as set up is not a definite dollar figure. It cannot be, because a contingent liability may be $500,000 or it may be 5 billions, against a 10-billion-dollar issue, so that from a bookkeeping standpoint it is utterly——

Mr. Luce. I will modify my statement by putting in the word "potential."

Mr. Harvey. I should say no, definitely no, because the country cannot get on without at least 10 billion dollars of circulating demand deposits and currency combined; in fact, it cannot get on satisfactorily with less than thirty or forty billion dollars.

Mr. **Luce**. That is a question of desirability. I am talking simply about the bookkeeping entry.

Mr. Chairman, that is all.

Mr. **Crawford**. May I ask a question?

Mr. **Goldsborough**. In answering Mr. Luce's question, the difficulty probably is that you were speaking in terms of goods, while Mr. Luce was speaking in terms of money. If this interbank currency which is set up primarily on the books as 10 billion dollars is used for the purpose of creating a price discount, and therefore an expanded market, and if the result of that is that the people get more of the good things of life, more goods than they otherwise would have gotten, do you say then that society, or the Government which represents society, has lost any part of the 10 billion dollars?

Mr. **Harvey**. No, sir; not at all.

Mr. **Goldsborough**. They have gained, haven't they?

Mr. **Harvey**. They have gained that much. They have not lost it. They have justified the issue of the money.

Mr. **Luce**. May I comment on that by saying that that is true with respect to these other entries covering the home-loan banks and all of the other activities concerned—the home-loan banks, the Farm Credit Corporation, Federal Housing, all of these agencies that are expected to do good and which were put there for the welfare of the country. But I have been addressing myself throughout entirely to the financial aspect of the situation, attempting to understand what would be the significance of adding 10 billion dollars to our contingent liabilities.

Mr. **Harvey**. Of course, it would not appear on the Treasury's books in the form of a contingent liability—I missed that point—because it would be there as a credit and a debit to the banking system. That is the way that it would stand on the books of the Nation.

The **Chairman**. What about the exchange of interbank currency with the Secretary of the Treasury for regular currency?

Mr. **Harvey**. The object of that is, of course, to establish the credits which arise through the retailers on a basis equivalent to the deposits now existing, that will exist in another form. The banks are liable to pay cash out against a deposit for the expansion of credit that they make themselves, and it is therefore logical that where cash is required and the bank is short of cash, the expansion of credit by the Government in this form should be honored to the extent that the public desires currency, and I think it is perfectly certain that the effect of this increased flow of business through the banks would tend to reduce the amount of currency in circulation and the demand for it.

At the present time, for some reason or other, we have a very much larger volume of currency in circulation than is normally necessary.

The **Chairman**. But what I am inquiring about is the operation of the bill which seems to contemplate the exchange of interbank currency for regular currency, whatever it may be, with the Secretary of the Treasury.

Mr. **Harvey**. Only in the case of emergency.

The **Chairman**. I understand that it is only in case of emergency, but I am wondering just what is contemplated and expected by that provision of the bill.

Mr. Goldsborough. Mr. Steagall wants to know when that provision of the bill would go into effect.

The Chairman. Yes; and what is expected of it.

Mr. Harvey. It would go into effect——

The Chairman. That is a thing separate and apart from the general mechanics of this bill, and I am just wondering what the purpose of that is, and what is expected.

Mr. Harvey. I think, Mr. Chairman, that it would go into effect if banks got into difficulties, but not otherwise. As I said in that respect, it supplements the deposit insurance to the extent of the Government's guarantee of a circulating medium.

The Chairman. I do not see how you could figure it that way, because you do not treat your interbank currency as a part of our circulating medium.

Mr. Harvey. Oh, yes, sir.

The Chairman. That has been in a class by itself.

Mr. Harvey. The credit that it gives rise to is the circulating medium, and the currency circulates through the banking system to support it. In other words, it is the collateral that goes through——

The Chairman. The only point that I am raising is that this provision seems to establish a method by which interbank currency may be turned in by any bank that happens to have it, to the Secretary of the Treasury, and exchange it for national currency.

Mr. Harvey. But only if it is in trouble.

The Chairman. I understand that it applies to cases of emergency.

Mr. Harvey. It may be that that clause may be unnecessary.

The Chairman. It may be unnecessary, or it may be very necessary.

Mr. Harvey. Yes, sir.

The Chairman. But I am wondering how it will work. It seems to me that it would be in the nature of an invitation to any bank holding interbank currency to consider itself in distress in order to make the exchange.

Mr. Harvey. If it deliberately created a run on itself in order to get that money——

The Chairman. But you do not say that it would have to be a run. You just say, as I understand it, that there must be an emergency, and the bank itself is to be the judge of it.

Mr. Harvey. No; I think it says that the Secretary of the Treasury may do it.

The Chairman. That is true, but I am talking about who decides whether there is an emergency or not. The bank decides that there is an emergency, and calls on the Secretary of the Treasury, and the Secretary of the Treasury may make this exchange?

Mr. Harvey. The Secretary of the Treasury will reply, "My investigators say that you have no emergency, and that your quick assets are quite sufficient to take care of that situation."

The Chairman. Do you have any method by which you can tell what a Treasury official would decide to do under a statute which states that he may do something? You evidently have sources of information and knowledge that I do not have.

Mr. Harvey. The bill might be amended there to say that the Secretary of the Treasury shall be governed by the findings of the Federal Reserve inspectors of that particular bank.

The **Chairman.** Suppose that a bank did decide that an emergency existed, and called on the Secretary of the Treasury for the exchange of currency, and the Secretary, under the provisions of the bill, did make the exchange and the bank turned out to be insolvent. What would be the effect of that exchange?

Mr. **Harvey.** I tried to answer Mr. Luce on that subject. The effect of that exchange would be that the Government might or would lose the amount of the difference between the assets and the liabilities of the bank. In other words——

The **Chairman.** Whatever would be involved would be in the nature of a contribution on the part of the Government to the assets of that bank?

Mr. **Harvey.** Yes, it would.

The **Chairman.** Or an obligation to redeem the interbank currency?

Mr. **Harvey.** But only to the extent that the bank goes into debt to its depositors.

The **Chairman.** And to the extent of the amount of currency supplied by the Treasury?

Mr. **Harvey.** Provided that the emergency did exist.

Mr. **Ford.** Might I make an observation at this point?

The **Chairman.** Certainly.

Mr. **Ford.** In discussing the interbank currency, there is one phase of the bill that bothers me, and that is this: We start out with a 15-percent discount, credited on the proposition that consumption is 15 percent behind production, and that the people are unable to buy, and therefore the discount is permitted, and this 15-percent discount permits the consumers of goods to take up that slack. Then we get to the point where production and consumption are balanced, and immediately upon coming to that point, the board would declare the discount out, so that it would not be effective again until such time as that slack beween consumption and production came on again. That seems to be the philosophy of the bill. It does not mean that you will get 15 percent at all times. The board might say that it should be a 3-percent discount, because they found that there was a slack of only 3 percent between consumption and production, and it might be 1 percent, and at any time that a parity is obtained between consumption and production, the discount ceases immediately and therefore the contingent or any other kind of liability ceases, but there is still a question to be answered that during the period of that 15-percent take-off, there has been 6, 7, or 8 billion dollars of interbank currency issued to the various banks, and they have it in their vaults. They cannot distribute it. It is there. Now, production is on a parity, and I am wondering if it is fair to give a consumption bonus, and if the time comes when consumption outruns production, would it not be a sane provision to have a consumption tax on the fellows who were getting 15 percent on a bad market? It seems to me that they could afford to pay the bank enough on a good market to make that difference up, and let that go back and readjust any contingent liability that might be created on the Treasury's books.

Mr. **Goldsborough.** May I interpose?

Mr. **Ford.** Yes.

Mr. **Goldsborough.** I want to say that the suggestion mentioned by Mr. Ford was contained in the bill originally introduced in December 1935, but in the discussions the discount was referred to as an inverted sales tax which could be converted into no tax or into a national sales tax in case it was found that too much money was getting into circulation. In this bill, in view of the universal antipathy of the people to a sales tax, we thought it sounder to have a provision for the recall of interbank currency, rather than a sales tax. That is what happened.

Mr. **Ford**. When you can call on a bank for $100,000, for instance, of interbank currency, what do you give it for the $100,000 that it has received? It has not received anything for the liability that it has assumed except that $100,000 on its books of deposit.

Mr. **Goldsborough**. Well, the bank's ability to loan on its fractional reserves is reduced to that extent. That is the only thing that happens to the bank.

Mr. **Ford**. But just a moment ago we were told that the 15 percent did not go to the fractional reserve, that if a man had $100,000 on his books, $85,000 actually deposited and $15,000 in interbank currency, that that $15,000 did not affect his reserve.

Mr. **Goldsborough**. But in order to return the interbank currency to the Treasury, he would have to reduce his fractional reserve in order to get the money in and to return the interbank currency. That would reduce his general reserve ability.

Mr. **Ford**. What you are doing is that you are predicating the proposition on the fact that interbank currency can be given to a bank to make up for its lack of deposits, that is, to increase its deposits arbitrarily, and when consumption and production have balanced, then, in order to stop inflation, he will reduce his reserves to a sufficient amount, and by the amount he reduces them he will return that interbank currency to the Federal Treasury?

Mr. **Goldsborough**. That is correct; and the justice of that is this, that as production and consumption are being kept at a maximum, the banks will be receiving, because of the increased business and increased borrowing, all of the profit that it could possibly get anyway. It is of interest to the banks to keep consumption and production up to the maximum. The greater that consumption and production are, the more demand there will be upon the banks for sound loans, and ultimately this will be to their interest, even though they might have to return this interbank currency upon occasion and reduce their ability to loan to that extent.

Mr. **Ford**. Now, let me think that through a minute. Let me see if I get it. I can appreciate the moral side of that. If we are going to set up a system that will enable the banks to make profits in considerable excess of what they are making at the present time, then, as the result of that, after the business has rolled around and their coffers are piled up, then we are assuming that, in order to get those profits, they are willing to risk repayment to the Government of this interbank currency and reduce their reserves in perhaps an amount of 2, 4, or 6, or up to 15 percent, and that they are warranted in doing that by the excessive business that this would bring to their banks. I am assuming that that is a sound assumption; that if production and consumption were balanced there would be an increase in the volume of transactions, an increase in the banking business, an increase in all business, and a general increase of all profit, and as the result of that the banks would feel that they could afford to make good this contingent liability of the Treasury brought about in giving them this money at the time when it was needed and then return it and reduce their reserves to that extent.

Mr. Goldsborough. Yes.

Mr. Crawford. May I ask Mr. Ford a question?

Mr. Ford. Certainly.

Mr. Crawford. Does not subsection (c), on page 4, prohibit that from operating until the difference between production capacity and consumption exceeds 15 percent? You keep referring to 2, 3, 6, or 9 percent.

Mr. Ford. I did not get it that way. Maybe it does. I would like to ask Mr. Goldsborough that. My conception of this bill is this, that there is a general acceptance today of the fact that production is ahead of consumption.

Mr. Goldsborough. You mean potential production?

Mr. Ford. Yes. We talk about there not being enough money in circulation, of there not being enough men employed, and that there is a piling up of goods that is detrimental to everybody. If we can get hold of some system that will enable the general public to purchase those goods by reason of lower prices—and that was Ford's theory all the time; not mine, but Henry's—we can keep the rhythm going and keep production balanced with consumption.

Now, keeping production balanced with consumption would be a useless thing unless we kept maximum production or potential production up to a point where everybody could buy everything that was produced, and what the people need to buy these things is enough money, and if we can get this country to a point where every man, woman, and child in the United States can buy everything that he needs——

Mr. Goldsborough. Everything that can be produced in the country.

Mr. Ford. Or any place else, so far as that is concerned; we have to buy coffee and tea and other things outside, but if they can buy the things that they need, and have the money to do it, and if there is a faint suspicion of a possibility of that being accomplished by this bill, then it is a good bill. If there is not, if it is going to be tied up in a lot of technical administrative things that will check it, it would not be a good thing, but if that can be acomplished, that is the thing that every thinking economist or every man who has the best interests of his country at heart today wants to happen, and that, I think, is what you are trying to accomplish.

Now, the question arising is, Will this bill do that? If any provision of it will aid in doing that, or if by amending it one way or the other it will in the end take a step in that direction, it will be a good thing.

Mr. Crawford, you spoke of——

Mr. Goldsborough. Subsection (c) on page 4.

Mr. Crawford. May I say this? Insection 4, on page 3, subsection (a), there is a provision that the discount shall be proclaimed. Section (b) provides that until that is proclaimed, 15 percent shall govern. Section (c) provides that no proclamation shall be made—let me give you the exact language:

> **No retail discount shall be declared unless productive capacity, ascertained as above described, shall exceed consumption by at least 15 percent.**

There has been so much reference made to rates less than 15 percent that I want to get into the record whether or not 15 percent is to govern, or something less than that.

Mr. **Goldsborough**. The reason that was put in was to avoid the objection that the bill was inflationary. Of course, the bill can be amended in any way that the committee might see fit when it is ready to consider it.

Mr. **Ford**. I should think that the larger the discount, the more dangerous it would be from an inflationary standpoint.

Mr. **Goldsborough**. This bill says that you cannot have the discount at all unless it is ascertained that the productive capacity exceeds the consumption capacity by at least 15 percent, and that was put in there for the purpose of trying to prevent any inflation.

Mr. **Ford**. That 15-percent margin is the thing that breaks prices, breaks everything.

Mr. **Goldsborough**. I think the margin now is 50 percent.

Mr. **Ford**. I do not think so.

Mr. **Goldsborough**. However, that can be changed.

Mr. **Ford**. The idea is to balance production and consumption?

Mr. **Goldsborough**. Yes.

Mr. **Ford**. Of course, that can probably never be obtained, because statistics, be they ever so correct, could not be followed closely enough to do that, but if it were kept within a reasonable basis, and whenever it was found that there were excessive goods the discount rates were applied to take them up, I think that would probably have a tendency to solve the situation, at least in a measure.

Of course, most of the members of the committee seem to be puzzled about the solvency of the bank currency. That seems to be the thing that is getting them. May be it is not currency at all, but purely a credit authority on the part of the Treasury, to keep the bank books in balance with their deposits.

Mr. **Goldsborough**. May I just take a minute or two on that?

Mr. **Ford**. I want you to take all of the time that you want.

Mr. **Goldsborough**. Under this bill, this Government agency that is created—we will just say the Government—would say to the banks, "Here, we do not propose to interfere with your business at all. We propose to let you conduct it exactly as you are now conducting it, but we are asking you to also conduct, as our agent, a supplementary work. We propose to deposit with you as trustee, from time to time, enough money to take up whatever the discount may be, which is determined by the Federal Credit Corporation, and we propose to allow you a service charge for performing that service, and we propose to allow you also, in view of the fact that you have allowed the retailer to put a corresponding amount on your books for deposit, to loan to the borrowing public, your customers, that same amount dollar for dollar.

Mr. **Reilly**. Of interbank currency.

Mr. **Goldsborough**. No; of actual loans.

Mr. **Reilly**. That is no privilege. They have that now.

Mr. **Goldsborough**. No; they would not have the privilege now of loaning against this interbank currency. This bill gives them that privilege, of loaning against this interbank currency, dollar for dollar.

Mr. Reilly. But what good would it be unless they cannot loan the interbank currency? The banks would be filled up with interbank currency that they could not loan.

Mr. Goldsborough. They can loan an amount equal to the interbank currency which they have on their books.

Mr. Reilly. In other words, they can use the interbank currency, which is a reserve, to loan out?

Mr. Goldsborough. That is one way of expressing it.

Mr. Reilly. But the banks have not got it. If this bill had been in execution in 1929, we would have needed about 7½ billion dollars of interbank currency in that year.

Mr. Goldsborough. Let us assume that this bill had been a law in the latter part of 1929. When the loans began to be called in, unemployment started, and prices began to fall, this retail discount would immediately have come into operation, and could have been expanded indefinitely, until buying power had reached the masses of the people. As soon as it did that, and they began to buy, and production began to expand, confidence would have been restored, and probably a very small part of this $10,000,000,000 would have been needed in order to restore confidence, to restore business to its normal condition.

Mr. Reilly. But suppose that it was $5,000,000,000 that was needed; what are the banks going to do with that, outside of reserves? My recollection that you made the statement that this was not an inflationary measure.

Mr. Goldsborough. Correct.

Mr. Reilly. It becomes inflationary just as soon as you permit the banks to loan money that they now keep as reserves. Just as soon as you permit a bank to go into its reserves, or to go into interbank currency in their place, you have that much inflation.

Mr. Goldsborough. Probably I do not understand.

Mr. Reilly. Stated in another way, let us assume that today the banks have $5,000,000,000 in reserves. They have not got it, but we will say that they have. Now, they have to keep it in the bank, and they cannot lend it. If you issue this interbank currency until you get to $5,000,000,000, they could put that in the place of the reserves, so that they can increase the circulating medium $5,000,000,000.

Mr. Goldsborough. In the first place, let us assume that in putting out this $5,000,000,000, they have increased the goods of the country to the extent of $5,000,000,000. There is certainly no inflation there, because you have goods corresponding to your money. As long as you do that, you do not have inflation.

Mr. Reilly. I see what you mean.

Mr. Goldsborough. That is the first proposition. The second is this, that under this bill, the Federal Reserve Board would have the right to increase reserve requirements up to 100 percent, so that if any inflationary condition did arise by the operation of this law, the reserve requirements could be raised.

Those are two answers to your question.

Mr. Reilly. Then the fact is that it is an inflationary measure, because you are taking the precaution to provide that the Government shall step in and prevent inflation.

Mr. Harvey. Mr. Chairman, may I say something?

Mr. Reilly. Just one moment.

Supposing that you put this bill into execution next year, and the discounts amounted to 8 billion dollars. What assurance have you that that 8 billion dollars that they have in discounts will be spent? If I go down and get a 15-percent discount, you have no assurance that I will spend that extra money. I may put it in the savings account. The only people that you can expect this to work with are those who live on the border line, who need every dollar that they collect. If a farmer buys a threshing machine, and he gets a discount of 15 percent, he will not buy another one. He just saves that much on this one.

Mr. **Goldsborough**. Of course, your statement is based on your conception of what might be the reaction of human nature. My conception is entirely different. I think that people now have a much greater tendency to spend than they did 5 years ago, and that 5 years ago they had a greater tendency to spend than 10 years ago.

Mr. **Reilly**. No question about that at all.

Mr. **Goldsborough**. And I think that the more opportunity you give them to get the good things of life, the greater the desire becomes to procure the good things of life, and the more apt they are to spend.

Mr. **Reilly**. You have no assurance what percentage of that credit would be spent.

Mr. **Ford**. Eighty-seven and a half percent of all the goods and services purchased in the United States are purchased out of pay checks.

Mr. **Reilly**. That does not affect the question of how many people will spend what they get through this discount.

Mr. **Ford**. The pay-check fellow spends all he gets.

Mr. **Reilly**. But the man with the salary, or the man with a good income, cannot be expected to buy any more than he would ordinarily buy, and he would put his discount aside.

Mr. **Ford**. No; he would be able to buy 15 percent more than otherwise, and 87½ percent of all the purchases of goods and services of the United States comes from pay checks.

Mr. **Brown**. I have a question.

Mr. **Goldsborough** (to Mr. Harvey). Do you want to answer Mr. Reilly?

Mr. **Harvey**. I thought that I would like to say this, and that is that the word "inflation" has been very much abused, and a new word has been substituted for it to meet the real situation that we have been confronted with, and which has been the policy of the Government, and that is "reflation." This is a question of reflation. We are trying to get money in circulation, up to what it ought to be to make the income per capita equal to that of 1929 available to the public, and that is what the gage of this money is. It is probable that 10 billion dollars would not be needed, because the flow of your money is three times a year, about. Therefore, if you want to increase your national income by 10 billion dollars, and if you can keep in circulation 3½ billions, you are going to get your 10 billion dollars increase in income.

I tried to show in my paper the reason why the 20 billions of dollars that the Government has already put out to do that has only resulted in a dollar-for-dollar increase in income, whereas by lowering prices to the consumer, and allowing the general wholesale price level to follow its own line upward, you will get the circulation that otherwise will not be gotten and cannot be gotten by our present methods of trying to prime the pump, because you are pulling from the other end of the string by means of your reduced retail price and you are leaving the profit system exactly as it was in 1929.

That is what I was trying to cover. It is not an inflation, but inflation might come, and it might come in exactly the way that Governor Eccles explained to this committee not very long ago, that the Federal Reserve Board was afraid it might come, and the President has been afraid it might come that way, and that is by ungoverned expansion of credit on the fractional reserve system of banks, which is what happened during 1923 to 1929.

I am trying to explain the philosophy of the monetary mechanism behind this bill to you, because I think that that monetary mechanism is a correct mechanism, a correct interpretation of the way in which money flows and creates wealth.

Mr. **Ford**. At that point, is it not true that the tremendous expansion that occurred in 1929 was because money was not going into industry and commerce for the expansion and reproduction of goods, but was going into speculation on the market?

Mr. **Harvey**. Yes, sir. It was being withdrawn from expendable income, and put into speculative securities. That the Brookings Institution shows very clearly indeed.

Mr. **Ford**. And this is an attempt to stop that by making it more profitable to purchase goods than to purchase securities?

Mr. **Harvey**. Yes.

Mr. **Luce**. One more question. Page 13, subsection (d), reads:

> Interbank currency notes shall be accepted for all forms of Federal taxation payable directly by the banks, and may be used by them as bank reserves, dollar for dollar, but not as a medium for expanding private credit in the form of loans built on fractional reserves.

What is the justification for having the Government lend money to the banks to pay their taxes?

The **Chairman**. That is the question that I was about to ask.

Mr. **Harvey**. I do not quite understand the question. I did not know that the Government would be lending money to the banks to pay their taxes.

Mr. **Luce**. They are allowed to pay their taxes in interbank currency, which we have recognized to be money in the hands of a trustee, as you have explained. Now, why should the Government lend to a trustee, money with which to pay taxes back to the Government?

Mr. **Harvey**. It might be very convenient, and might be necessary, to call in this currency and use it for maintaining the flow of goods through the discount, by bringing it from an inflated volume of bank credit, and putting it back into the same consuming buying power. It might be necessary to do that, and probably will be from time to time, but the more of this currency that comes back into the hands of the Government, the less it will have to disturb the general credit operations of the bank, and therefore that clause was put in merely as a sort of side issue, to allow the banks to divest themselves of some of that currency, if they preferred to issue their own credit instead.

Mr. Luce. It does not seem to be logical for the Government under any circumstances to give banks the abnormal privilege of paying back to the Government money that the Government lends to them and therefore changing the status of the bank as a debtor of the Government. This permission would be available to a bank, for instance, that could well afford to pay its taxes in the ordinary way.

Mr. Harvey. Yes, sir; anf if it paid that way, it might not be nearly so good for the general economic condition of the country as if it paid in the return of interbank currency notes.

Mr. Luce. But you do not make it obligatory.

Mr. Harvey. It is permissive.

Mr. Luce. And it may or may not be consonant with the general purposes of the bill.

Mr. Harvey. Well, of course, it seems to me that the judgment of the committee will be relied upon to meet that situation with any amendments or modifications that they may decide upon.

The Chairman. If you give these banks permission to pay their taxes in money of this kind, would not the tendency be for all the banks to use that money for that purpose?

Mr. Reilly. And what would the Government do with it when it got it?

The Chairman. And what would the status of the account between the Government and the bank that used this money for the purpose of paying Government taxes be?

Mr. Harvey. The Government would reduce the outstanding amount of interbank notes.

The Chairman. Yes; it would reduce the amount of outstanding interbank notes to the extent that it is employed for the payment of taxes, because the Government would not use it for any other purpose unless to put it back into the interbank currency fund, but I am talking about a transaction where the bank uses interbank currency to pay taxes. Wouldn't that be a way by which that bank could avoid paying taxes?

Mr. Harvey. Well, I do not know that you could interpret it that way. If a bank has issued circulating deposits against that interbank currency, and it has sufficient reserves to carry its deposits without using the interbank currency as a 100-percent reserve against a portion of them, then it would be, under the bill, at perfect liberty to use the interbank currency to pay its taxes to the Government, and the Government would be in the position of having recovered part of that currency, which it would have in reserve for use again at the consumers' end of the monetary cycle, which would be a great advantage to the Government, because it would not be compelled to call in currency to the extent that it had received it in taxes, and therefore would not be compelled to reduce outstanding circulating deposits. It is not essential, sir, to the bill.

The Chairman. I am wondering if that fits in.

Mr. Spence. When the beneficiary of the discount deposits his money, there is 15 percent added to his deposit, is there not?

Mr. Harvey. Yes, sir.

Mr. Spence. And the bank is indebted in the full amount to the depositor?

Mr. Harvey. Yes, sir.

Mr. **Spence**. Then the depositor can do with that as he pleases?

Mr. **Harvey**. Yes.

Mr. **Spence**. The bank has no control over that. The depositor can check against that for the full amount, can he not?

Mr. **Harvey**. Yes.

Mr. **Spence**. Suppose that he does check against it for the full amount, and the 15 percent is reimbursed to the bank by the interbank currency, and then later the Treasury withdraws the interbank currency. What happens to the bank?

Mr. **Harvey**. The bank, of course, would have only about 15 percent of interbank currency against its total resources, and probably even less than that, if you add in its investments. If it is found impossible to reduce those deposits, because there is too rapid a rise in prices and a demand for credit from the investing public, then if that currency is called in, it reduces the general level of deposits, and banks will have to increase their surplus reserves in order to meet the demand of the Government to return the interbank currency by calling speculation loans or they may sell securities which they have purchased and against which they have issued their own credit, or they may recall some of their security loans. The market may be going too high; the banks may feel that the market is going too high, and they would be glad to have a hint from the credit authority to call in some of the loans, because the banks do not like to call in these loans. I know that, because I have been on a board of directors when that question has come up.

Mr. **Spence**. But that 15 percent has increased the deposits of the bank, and its liability to the depositors 15 percent.

Mr. **Harvey**. Yes.

Mr. **Spence**. Just as much as any legal-tender deposit would increase it.

Mr. **Harvey**. Yes.

Mr. **Spence**. And when you take away the interbank currency, why does not that bank sustain as great a loss as if you took that much legal tender from the bank? I cannot see any distinction there.

Mr. **Harvey**. It works in exactly the same way as if you had $1,000 in the bank and drew it out in currency, or by drawing a check.

Mr. **Goldsborough**. I wish you would go into details about that, because that is giving the committee more trouble than anything else. Just explain that, please.

Mr. **Spence**. Let me ask him this: Is it not, in effect, a deposit by the Government of 15 percent, to the credit of the depositor?

Mr. **Harvey**. That is what it is.

Mr. **Spence**. And when you destroy that 15 percent by the recall action of the Treasury, do you not just wipe that out?

Mr. **Reilly**. They have to pay the bank real money when they recall this interbank currency; otherwise a banker would not pay it. When the Government recalls your money, it must pay the banks real money.

Mr. **Harvey**. I would like to ask why the banker should be paid real money when the banker has issued credit on what is not real money, because it is not real money that the bank issues. The banking system today cannot pay their whole deposits in real money, if there is a sudden demand. That certainly was the case in 1932.

Mr. **Reilly**. If they issued a call for 1 billion dollars of this interbank currency, won't the Government have to pay 1 billion dollars of real currency?

Mr. **Harvey**. They would if the public demanded it, but not if the banks demanded it.

Mr. **Spence**. Subsection (e) of section 301 provides—

> Upon the findings and advice of the Federal Credit Commission indicating that inflationary conditions are tending to arise, the Secretary of the Treasury is hereby authorized and instructed to recall from the banks such amounts of the interbank currency in their hands as may be necessary to establish and maintain monetary equilibrium.

How do they do that?

Mr. **Harvey**. They would call the money in from an inflated credit at one end and put it back into circulation for goods at the other. That is what would happen. There is a cycle there, you see.

Mr. **McKeough**. There is a 15-percent gap there.

Mr. **Harvey**. Yes; and that is what makes the flow coming in from inflated credit, capital goods, if you like, or any speculative proposition, and being put back into the purchase of goods again, so that the purchase of goods is kept possible, which establishes the warrant for sound capitalism—sound earnings. When credit is reduced and you have falling prices, this would reimburse your buying power, and you will not have the condition that we have been through.

Mr. **Williams**. Do you expect the bank to take this out of its other assets and pay the Government?

Mr. **Harvey**. What other assets?

Mr. **Williams**. When it is recalling this currency.

Mr. **Harvey**. Yes; what I would call its inflated assets, because those——

Mr. **Williams**. You would have, as you said awhile ago, to recall some of the credits that the bank has outstanding.

Mr. **Harvey**. Yes.

Mr. **Williams**. And you would have to dip into foreclosed farms and homes in order to get the money back into the bank when the Government recalls this interbank currency?

Mr. **Harvey**. It could not very well—it would not naturally, I mean——

Mr. **Williams**. The assets and the liabilities of the bank would not balance if you did not do that.

Mr. **Harvey**. They would not call in their long-term loans. They would call in their circulating loans, their loans on securities, their demand loans first.

Mr. **Williams**. But those are the assets of the bank. I do not care whether you call them short-term or long-term.

Mr. **Harvey**. But they are also the liabilities of the banks.

Mr. **Williams**. You would say that those are not the assets of the bank?

Mr. **Harvey**. I say that the collateral is the assets of the bank, but the money is a liability of the bank.

Mr. **Williams**. The deposits are the liability of the bank. The securities that the bank owns, of course, are assets.

Mr. **Harvey**. May I say this: That when banks recall loans, as they do, they do not affect, provided that their loans are good loans, their capital or reserves and surplus at all. Their own money remains just as it was, and that would happen in the case of the recalling of these interbank notes.

Mr. **Williams**. I cannot see why the Government itself is not paying that 15 percent.

Mr. **Harvey**. Is not paying that 15 percent?

Mr. **Williams**. Not paying it; yes.

Mr. **Harvey**. It is paying it in the sense that it is maintaining a volume of money. It is issuing a volume of money.

Mr. **Williams**. It repays the 15 percent that the bank has already paid out?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. And your books are now in balance?

Mr. **Harvey**. Yes; but the bank——

Mr. **Williams**. They have given that repayment of credit for 15 percent that the depositor has checked out.

Mr. **Harvey**. Yes.

Mr. **Williams**. And you have this interbank currency in there to fill up the gap?

Mr. **Harvey**. Yes.

Mr. **Williams**. And your books are in balance?

Mr. **Harvey**. Yes.

Mr. **Williams**. And everything is all right now?

Mr. **Harvey**. Yes.

Mr. **Williams**. Suppose that the Government recalls that 15 percent of interbank currency, what shape does that leave the bank in?

Mr. **Harvey**. The bank will simply reduce its loans.

Mr. **Williams**. And pay it out of its other assets?

Mr. **Harvey**. The bank will simply reduce its loan and get in——

Mr. **Williams**. That is all that there is to it, isn't it?

Mr. **Harvey**. When it reduces its loans, it gets this money, but that money is not a bank asset.

Mr. **Williams**. What is the reason why it is not the bank's money?

Mr. **Harvey**. Because it is not. It is money created by the bank on securities that somebody else owns.

Mr. **Williams**. But it is now in the bank, is it not?

Mr. **Harvey**. The money is, yes; but it has been created by the Government's interbank currency. Therefore the Government owns that money.

Mr. **Williams**. The Government takes that money back?

Mr. **Harvey**. Yes, sir. The Government owns that credit that was issued.

Mr. **Williams**. That money did not come from the Government which it got in the first place?

Mr. **Harvey**. The money comes from the Government through the issuance of credit. It did not come from the bank.

Mr. **Williams**. The bank does not make money simply out of whole cloth, does it?

Mr. **Harvey**. No.

Mr. **Williams**. It has assets back of it all the time. This thing of talking about bank credits being made simply out of thin air is not correct. The bank has to have back of that credit, if it is a sound bank, at all times assets sufficient to repay the money outstanding, does it not?

Mr. **Harvey**. Yes.

Mr. **Williams**. It seems to me that when you interject this interbank currency into that situation, you get the whole thing off balance.

Mr. **Harvey**. I would like to put a thought in your mind. It has these assets, and it has also these deposits, but it does not own either of them. It is merely a fiduciary agent in connection with them, and it has to see that the money that it has issued, and the collateral that it holds in trust, are equal at least. The same thing happens to notes——

Mr. **Williams**. You say that there is a fiduciary relation as to this interbank currency?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. And yet it is deposited in the banks and intermingled with other funds, and drawn out on check?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. And used to pay taxes?

Mr. **Harvey**. Yes.

Mr. **Williams**. What is the fiduciary relationship there? What is the reason it is not the same as any other fund? My idea of a fiduciary relationship, or of a trust fund, is that you have to keep that fund intact, and deliver it when you are called upon to do it.

Mr. **Harvey**. I have no doubt at all, sir, that if you feel that an amendment should be made to eliminate that tax clause, that the committee would accept it.

Mr. **Williams**. If you eliminate the 15 percent, you take out all that there is in this bill.

Mr. **Harvey**. If you eliminate the tax clause, it does not affect the economic principle of the bill at all, the monetary principle.

Mr. **Williams**. Is it your idea that this bill will reduce costs to the consumer?

Mr. **Harvey**. It will reduce costs to the consumer.

Mr. **Williams**. It will reduce the retail cost?

Mr. **Harvey**. Yes.

Mr. **Williams**. What will it do to the wholesale prices?

Mr. **Harvey**. It will leave the wholesale prices exactly as they are.

Mr. **Williams**. That is your idea of this bill?

Mr. **Harvey**. Yes. I have prepared——

Mr. **Williams**. Let me ask you this question. It will not reduce, in your judgment, the wholesale prices?

Mr. **Harvey**. No.

Mr. **Williams**. Is it not a fact that if the production is expanded to 100-percent capacity, that that will lower the cost per unit of production?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. Very materially lower it, will it not?

Mr. **Harvey**. Yes.

Mr. **Williams**. To the producer?

Mr. **Harvey**. Yes.

Mr. **Williams**. If that is true, why should not the wholesale prices come down?

Mr. **Harvey**. Under those circumstances, I think they would, but that is a competitive condition that this bill does not attempt to regulate.

Mr. **Williams**. If the wholesale prices are not reduced, and the cost of production is reduced, the wholesalers, the industries, and the factories of the country would be very materially benefited, and nobody else would.

Mr. **Harvey**. I think that the public would be benefited very much.

Mr. **Williams**. It would increase their profits very materially, would it not?

Mr. **Harvey**. It would reduce the cost of living and increase the profits of the producer.

Mr. **Williams**. I understood you to say that it would not reduce the wholesale costs.

Mr. **Harvey**. Only as it would competitively. I have covered that in an answer that I have prepared for Mr. Patman. Congressman Patman asked practically the same question, and if I may be permitted to read my answer, it will, I think, throw some light on your question.

May I do it?

Mr. **Patman**. Would you mind putting that into the record and let me ask you a question?

Mr. **Goldsborough**. I think that he ought to be allowed to read his answer.

Mr. **Harvey**. In answering questions of this sort one has to be very clear in his expression. I am not accustomed to talking very much on my feet, and I find that I can express myself much more clearly if I can write it down.

Mr. **Williams**. Let me ask you a question——

Mr. **Goldsborough**. Let him answer the other question first.

Mr. **Harvey**. Shall I read it?

Mr. **Williams**. He has answered my question, as I understood it.

Mr. **Harvey**. Shall I read it?

"Regarding the effect upon the prices——"

Mr. **Williams**. You do not want me to ask another question?

Mr. **Harvey**. Yes, sir. I will wait and read this later, but I think perhaps I can answer your question——

Mr. **Goldsborough**. Supposing that you answer Mr. Williams' question.

Mr. **Harvey**. Will you ask your question?

Mr. **Williams**. How many people are there, according to your study, unemployed in the United States now?

Mr. **Harvey**. As far as any record shows, it is somewhere between three and four millions.

Mr. **Patman**. How many?

Mr. **Harvey**. Between three and four millions.

Mr. **Williams**. This plan that you are proposing here puts everything on a cash basis, does it not?

Mr. **Harvey**. Up to the amount of the discount, it does; yes.

Mr. **Williams**. 85 percent all cash and 15 percent discount?

Mr. **Harvey**. The 85 percent would not be cash. The 15 percent would be cash.

Mr. **Williams**. How is that?

Mr. **Harvey**. The 15 percent would be cash. The 85 percent would flow just as it is flowing now. For instance, I carry——

Mr. **Williams**. I mean that the sale would be $85 in cash and 15 percent credit or discount.

Mr. **Harvey**. Yes.

Mr. **Williams**. Fifteen cents on the dollar would be credit or discount.

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. How would that reach the fellow who has nothing with which to purchase?

Mr. **Harvey**. Whatever he is getting from the Government would be increased by 15 percent. That is the way that it would affect him in the first place. Then there would, I think, be a greater demand for goods, which would increase production and put him to work. That is another place where he would be benefited. If there is a time lag before he goes to work, I think that the present method of taking care of him might be continued.

Mr. **Williams**. You want to increase consumption and production both?

Mr. **Harvey**. Yes.

Mr. **Williams**. Which will come first?

Mr. **Harvey**. Which will come first?

Mr. **Williams**. Yes.

Mr. **Harvey**. Consumption will come first.

Mr. **Williams**. Then you have to have the means to purchase with.

Mr. **Harvey**. Yes.

Mr. **Williams**. You have to have that, notwithstanding the fact that you have all of these men unemployed. It would not put another man to work in order to give him that increased purchasing power first.

Mr. **Harvey**. It gives him increased purchasing power when he buys goods. I do not know whether you would class that first or second.

The **Chairman**. We will have to adjourn until tomorrow morning at 10:30.

Mr. Harvey, can you come back for another meeting at the first of the week?

Mr. **Harvey**. Yes, sir; but not Monday.

The **Chairman**. We have another meeting scheduled for tomorrow.

Mr. **Patman**. May I ask one short question of the professor before he leaves?

Mr. **Harvey**. Not professor; I am a businessman.

Mr. **Patman**. I beg your pardon.

I have figured out the different retail establishments and the different concerns that would have to get a Federal license in order to operate under this law, and I want you to tell me whether or not I am correct in saying that the list includes those handling groceries, drugs, hardware, gas stations, garages, fruit stands, farmers' markets, cleaning and pressing shops, laundries, printers, newsboys and newsstands, electric light companies, water companies, telephone companies, gas companies, hotels, restaurants, lumber dealers, sawmills, plumbers, painters, carpenters, real-estate dealers, rental agencies, liquor stores, and theaters. Any of those would come under the terms of the act, and would have to obtain a Federal license, and there are three or four million of them, and it would take one person to supervise each store, on an average, and that would take up all of the unemployed, according to your estimate, and that would not count in the extra help that the retailers would have to add, or that the banks would have to add, to keep up with this, would it?

Mr. **Harvey**. I would not expect it myself to employ so many people to chase these retailers. I do not think that you would have to chase many retailers.

Mr. **Patman**. It would be up to them, and I would be reluctant to leave it to them.

Mr. **Harvey**. I am sorry that I did not have a chance to answer that other question.

Mr. **Patman**. Just put the answer in the record. Will that be all right, Mr. Chairman?

The **Chairman**. Yes.

(The answer referred to by the witness is as follows:)

Regarding the effect upon prices, or the general price level, Mr. Patman expressed the opinion that the intent or effect of this bill would be lowering the general level of prices. I cannot agree with this statement.

The purpose is to lower the prices of goods sold at retail, without affecting the general trend of prices of all commodities. The effect of the discount on prices at retail would be to increase demand and this would naturally tend to increasing the general price level, which is advisable.

The impact of competition would be the governing factor of the general price, as it is now. Retail prices would tend to rise, but the discount would offset this rise in relation to the general price level as far as the cost of living is concerned. Thus we would have a general "firming" of the price level. There would be more employment and a larger pay roll, which would further increase the demand for consumption goods.

This would be of immense benefit to general farming, because the farmer would buy his necessities and comforts at the lower retail price, while he would receive the higher ruling price for his products. He would thus benefit both going and coming.

As to ability of the truck farmers to sell their products direct to consumers, my opinion is that farmers who do this follow one of two courses. They either make a specialty of certain choice products and sell them regularly to consumers at a price higher than that ruling for standard products in the store, or else they offer their surplus to their customers at lower prices than prevail in the stores. Convenience of deliveries and the freshness of the articles sold make them desirable to the purchasers.

If one bases a forecast of the general trend of prices under the proposed enactment, and on previous experience, it may reasonably be assumed that the general price level would rise to about the average of 1924–29, and would become established there.

The reason for this is that in those years there was very free buying of commodities based upon a great expansion of credits, inflated monetary profits which arose from the rise in security prices and purchasing upon installments. These, together with the large pay rolls for production, offset the money withdrawn as savings, and we had something approaching equilibrium in the industrial field at a point about 20 percent below full industrial capacity.

This equilibrium was reached because the savings in cost due to large volume production left a comfortable, even liberal, margin of profits, and competition prevented prices and profits from being unreasonably kited.

The same thing may be expected to happen again, but the purchasing power that will generate it will not be of the unstable character that led to the end of that period, because it will be based on a monetary system not subject to sudden shrinkage and a credit system under better control.

But it will be the responsibility of the Federal Reserve Board and the Securities and Exchange Commission to prevent an inflation of securities and capitalizations which would cause widespread financial trouble if carried too far.

The **Chairman**. You say that you can be back the early part of next week?

Mr. **Harvey**. On Tuesday or Wednesday.

The **Chairman**. Tuesday, I should say.

Mr. **Goldsborough**. Mr. Chairman, Mr. Munson is here today and he can come back Tuesday, and if he does I think he ought to be allowed to make his statement.

Mr. Harvey, can you wait until he gets through?

Mr. **Harvey**. Yes.

The **Chairman**. That will be all right.

Mr. **Goldsborough**. Mr. Munson, will that be all right?

Mr. **Munson**. Wednesday will be better.

Mr. **Goldsborough**. Then we will let Mr. Harvey finish on Tuesday.

The **Chairman**. All right; we will meet again tomorrow morning at 10:30.

(Thereupon, at 12:18 p. m., the committee adjourned, to meet again Friday morning, July 23, 1937; and the hearing on H. R. 7188 was continued to Tuesday, July 27, 1937, at 10:30 a. m.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

WEDNESDAY, JULY 28, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., to resume hearings on H. R. 7188, Hon. T. Alan Goldsborough presiding.

Other members present: Hancock, Williams, Spence, Farley, Ford, Brown, Patman, Transue, Luce, and Crawford.

Mr. Goldsborough. The committee will come to order, please.

Mr. Munson, will you kindly come forward please, sir? Please give your name to the stenographer.

Mr. Munson. Gorham Munson.

STATEMENT OF GORHAM MUNSON, EDITOR, NEW DEMOCRACY

Mr. Goldsborough. Will you state your background for the benefit of the record, Mr. Munson?

Mr. Munson. Mr. Chairman and gentlemen of the committee, my name is Gorham Munson. I am a member of the faculty of the New School for Social Research in New York City. For 20 years I have been in magazine and publishing work. I have been a practicing journalist. As a journalist, naturally I have devoted a good deal of attention to public affairs, and in writing for magazines I have naturally had to devote a good deal of thought to economic questions.

In 1926 I became convinced that the fundamental defects in our economic system are to be found on the money side, and this morning I would like to read a brief which is divided into eight short sections, and, following that, to reinforce those eight points with supplementary remarks. May I have that permission?

Mr. Goldsborough. Proceed in your own way, sir, and if you prefer it, you will not be questioned until you finish your statement.

Mr. Munson. Yes; I would prefer that.

The first point is that H. R. 7188 crystallizes in its purposes the most progressive opinion in industrial and banking circles. A representative spokesman of this growing body of opinion is Mr. Vincent C. Vickers, late director of the Bank of England, who recently declared:

> As things stand today, money and the issue of credit is not controlled by the state, but by interested parties creating no real wealth, working to make money out of money—most of which is not theirs at all. What we want is not nationalization of banks—this would be quite useless and possibly fatal—but state control and state issue of credit, so that the money supply may be

> regulated solely for the benefit of the country as a whole, by a disinterested authority, and not with primary consideration given to the money business of financiers and bankers.

Unlike most money reform measures, H. R. 7188 is not divorced from enlightened industrial and financial opinion but is united with it in its general declaration of policy.

It is a bill to provide a national monetary policy in place of the policy of international finance to which governments are now compelled to adhere, and it is to be a national finance policy having a definite relationship to the requirements of domestic industry and trade under the conditions imposed by our power economy, a recognition of the basic fact that since the World War we have been living in the power age, successor to the machine age. Moreover, the bill declares the aim to increase production and consumption to the limit of the country's power to produce, and this emphasis upon the supreme economic importance of consumption, like the preceding emphasis on power economy and national finance, is one that is frequently made by industrialists with mass-production facilities.

Second, the technical provisions of H. R. 7188 for establishing a Federal Credit Commission and instituting the compensated price are derived from the economics of C. H. Douglas, Scottish engineer-economist. The analysis and proposals of Douglas have acquired a quite different standing in the world from the standing of other schools of monetary reform. The outcome of Douglas' considerable practical experience in industry and cost accountancy, the analysis and proposals have been before the world for 20 years and have stood the test of severe examination and criticism. In England, Canada, New Zealand, and Australia the Douglas ideas have entered the field of practical politics. H. R. 7188 thus stems from a ripened body of scientific thought concerning the economic problem of underconsumption and business depression in the midst of high productive capacity.

Third, H. R. 7188 is designed to remedy the continuous shortage of purchasing power which is mathematically inevitable under our present system of loan accountancy. This state of affairs has been summarized in a proposition commonly known as the A plus B theorem. The classic expression of the A plus B theorem is as follows:

> A factory or other productive organization has, besides its economic function as a producer of goods, a financial aspect—it may be regarded on the one hand as a device for the distribution of purchasing power to the individuals through the media of wages, salaries, and dividends; and on the other hand as a manufactory of prices—financial values. From this standpoint its payments may be divided into two groups:
>
> Group A: All payments made to individuals (wages, salaries, and dividends).
>
> Group B: All payments made to other organizations (raw materials, bank charges, and other external costs).
>
> Now, the rate of flow of purchasing power to individuals is represented by A, but since all payments go into prices, the rate of flow of prices cannot be less than A plus B. The product of any factory may be considered as something which the public ought to be able to buy, although in many cases it is an intermediate product of no use to individuals, but only to a subsequent manufacture; but since A will not purchase A plus B, a proportion of the product at least equivalent to B must be distributed by a form of purchasing power which is not comprised in the descriptions grouped under A.

It can easily be shown that this additional purchasing power not comprised under A is provided by bank loans and export credits.

Here is a simplified picture of this theorem of rate flow of prices and purchasing power as it operates in our economic life.

B, who is a manufacturer, borrows freshly created money from a bank which enables him to purchase from A a semimanufactured product. The money received from manufacturer B by manufacturer A repays A's bank loan and is thus canceled, leaving no deposit of new money in the name of either A or B. In the same way the goods can be financed to C, D, and so forth, and finally into the stores. The position now is that the retailers owe the banks money but the manufacturers are square.

Now note that in addition to the above loans manufacturers A, B, C, and so forth, will have borrowed to pay their workmen. This money in the hands of employees is all that is available to pay the price of the articles, that is, repay the retailers' bank loans. Owing principally to the lapse of time in serial production, a lapse of months to years, this money in the hands of consumers is insufficient to meet the price and the methods of funded debts must be employed to make up the deficiency.

Some foreign public body, let us say the Russian Soviet Government, is persuaded to issue bonds. Banks, either directly or through loans to speculators, are prepared to create new money and purchase these bonds. This new money is used to buy the goods, such as machinery, which are sent to the Russian Soviet Government in exchange for the bonds. These capital goods, which are always surplus to the purchasing power of the home consumer proper, are bought and sent abroad, but the wages for making them are distributed here. These wages are available for spending in the stores for consumer's goods. The retailers can now get the money and repay their loans, which cancels the amount and there is no money left in existence in respect to that cycle of production.

To put the whole matter briefly, the retailer can only be cleared so long as capital production increases.

This simplified picture has been drawn to bring into prominence the all-important time factor in economic life. The physical sciences for some time have been interested in the study of the rates at which processes occur. Douglas, bringing economics abreast of the physical sciences, has studied the rates at which prices are generated and incomes are given off in the same cycle of production, and he has discovered a discrepancy between these rates, which results in the home population never being able to claim the total goods they have produced.

It is this question of rates that makes the A plus B theorem seem so difficult and elusive and has brought into existence a considerable literature of interpretation and commentary. But the theorem has never been refuted, and in recent years there has been more and more agreement that there is a deficiency of purchasing power to meet aggregate costs.

H. R. 7188 implicitly recognizes the fact that current incomes cannot meet current costs and adopts the only sound method thus far proposed for equating consumption to production.

Fourth, the one sound scientific method for planning, organizing and raising consumption to production is the method of consumer-credits utilized by H. R. 7188. Our present financial system is not self-liquidating and can never be made self-liquidating by any scheme relying on repayable producer-credits. Producer-credits are debts and must be collected through prices and paid off. It is a piece of homely wisdom that we cannot borrow ourselves out of debt. The economic problem is insoluble so long as we adhere to what is known as the old or orthodox economics, with its principal assumption that production automatically finances consumption. In practice this assumption has been proved false.

H. R. 7188 crosses the gulf between the old and the new economics, which begins at the consumption end and maintains that if consumption is financed, production will take care of itself. H. R. 7188 recognizes that the purpose of production is consumption, and that the consumer is the economic partner of the producer.

To put the matter in a simple picture: The ship of society is powered by twin engines, production and consumption, driving twin screws, but only one of these engines, namely, production, is properly fueled. The feed pipe to the other engine has not been connected, and it works weakly on what power it can derive from production. It is no wonder that the ship is driven in a circular course of inflationary storms and deflationary doldrums, and it will continue to gyrate in circles until the consumption engine is properly fueled and the ship can then drive straight ahead.

H. R. 7188 will feed the credit power directly to consumption and enable it to pull together with production. It proposes an initial retail discount rate of 15 percent and the gradual raising of this discount rate as conditions warrant, thus directly augmenting the buying power of the American people.

The bill thus provides for a cautious, conservative, highly controlled, very gradualistic application of a radical financial principle. The initial retail discount rate is to be only 15 percent, although responsible social credit opinion generally endorses an initial rate of 25 percent. There is to be no retail discount rate at all unless productive capacity shall exceed consumption by at least 15 percent. Nor can successive retail discount rates be proclaimed which exceed the next preceding rate by a figure of more than 5 percent. H. R. 7188 provides ample safeguards against a too sudden acceleration of production and consumption. It will give the Nation ample time to adjust to a rising standard of living and prosperity.

Fifth, title III of H. R. 7188 is concerned with interbank currency and bank-credit control. It is a great improvement upon title IV in H. R. 31, a somewhat similar bill introduced at this session of Congress, which proposed a totally unnecessary credit-certificate retirement fund and other measures to be employed against a hypothetical undue monetary expansion. Title III limits the total amount of the initial issue of interbank currency notes to $10,000,000,000. They may not be used by the banks as a medium for expanding private credit in the form of loans built on fractional reserves. The Secretary of the Treasury, upon the findings and advice of the Federal Credit Commission indicating an inflationary tendency, is empowered to recall from the banks such amounts of interbank currency as may be necessary to check inflation.

In essense, H. R. 7188 is a counterinflationary bill. Rising prices are the characteristic mark of inflation. The compensated price, however, is a reduction of retail prices—an ingenious anti-inflationary method of augmenting the supply of purchasing power.

There is absolutely no danger that consumer credits will pile up and litter the financial landscape. As our productive system is called on to produce more, more money will be required to distribute the goods. Moreover, industry and agriculture are heavily in debt, and the liquidation of this vast debt structure will be a most effective brake on any conceivable inflationary tendency.

The central point is that under the economic system of Douglas consumer credits are automatically canceled. H. R. 7188 in reality provides for a method of canceling costs by consumer credits. It is designed to neutralize the effects of the A plus B theorem.

In the words of a social credit technician (Mr. R. L. Northridge):

> If that theorem is true at all, it is true continuously. So long as the present system of industrial accounting is maintained (and social credit, at least, does not propose to alter it) so long will it be impossible to recover in full each cycle of production credit. It will therefore not be sufficient to liquidate industry's present debt by an issue of consumer credit; every future production cycle will require a fresh issue of consumer credit if the production credit initiating it is to be recovered in full. In other words, every future production cycle will produce an increment of debt, i. e., "cancelation power," and it is this continuous stream of cancelation power that is the justification for a continuous stream of consumer credit and the guarantee for its cancelation * * * the question of special machinery for retiring consumer credits does not arise at all, if their issue is properly related to the ascertained deficiency of purchasing power.

Sixth, the proposal for economic rectification made by social credit is threefold: The opening of the national credit office, the institution of the compensated or assisted price, and the inauguration of national dividends. H. R. 7188 has equivalents for the first two but omits the national dividend device. In this it differs from H. R. 31, already referred to in this brief as a bill resembling in many ways H. R. 7188. Section 8, title I, of H. R. 31 provided for a national consumers dividend.

From the standpoint of technical economics, the omission of the national consumers' dividend is quite acceptable. The efficiency of H. R. 7188 as a technique for improving business conditions, drawing on unused productive capacity and elevating the Nation's standard of living is not impaired by leaving out the dividend. Considered as an economic measure designed to clear the retail market of goods and services that cannot now be sold, the bill is technically sound and feasible.

From the standpoint of political economy, however, the inclusion of the national consumers' dividend is desirable. By political economy is meant the broad policy which a specific act of economic legislation is designed to carry out. The broad policy of social credit economics is the security and liberty of the individual citizen, whether in or out of employment. The national consumers' dividend is a technical device for insuring the eventual economic independence of each citizen. The idea behind the dividend is, roughly, this: It is possible to conceive of the Nation as a kind of holding company known as the U. S. A., Inc., which does not interfere with the numerous smaller undertakings within the Nation but does issue additional purchasing power on the credit of all of them and distributes this as dividends to the shareholders who are the citizens of the Nation. It is a way of monetizing and distributing the unearned increment of association, which arises from the associated enterprises of our Nation.

The incorporation of this device in such a bill as H. R. 7188 would be an absolute guaranty against any possible frustration or perversion of the impulse toward economic democracy. It would, so to speak, place the center of gravity of the bill in the rights, well-being, and liberty of the individual citizen. The compensated price is a means to distribute abundance; the national dividend is a means to distribute personal liberty. The two devices together instrument the policy of abundance and freedom for all, which is the highest aim of political economy.

Seventh, suitable penalties are provided in H. R. 7188 for retailers who violate their contracts with the Secretary of the Treasury and for officials and employees of the Federal Credit Commission who violate their duties. There are no great administrative difficulties in enforcing H. R. 7188.

In one important respect, however, it appears to the writer that H. R. 7188 is seriously deficient, and that is in respect to price control. Credit issue and price making are the positive and negative aspects of the function that controls the economic life of the community. H. R. 7188 democratizes credit issue, the positive aspect. It introduces the principle of the ratio in the negative aspect, price making, but it contains no profit-regulating clause, no control device to safeguard against profiteering.

It would seem that the framer of the bill is confident that the free and genuine competition which would come to pass were the bill enacted would be sufficient to keep profits reasonable, and there is no doubt that healthy competition could be considerably relied upon to restrict profits. Nevertheless, profiteering habits are ingrained, and the tendency to monopoly capitalism is powerful.

The writer is strongly of the opinion that a bill like H. R. 7188 should contain a clause protecting the consumer from exploitation by profiteers and monopolists of commodities. A clause modeled upon the following, which is taken from the Draft Social Credit Scheme for Scotland, would seem to be adequate:

> The conditions of such registration (to dispense the retail price discount) will be that their accounts, as at present required under the companies acts, should contain an adidtional item showing the average profit on turn-over, and that their prices shall, as far as practicable, be maintained at a figure to include such average profit, where this is agreed as equitable for the type of business concerned (the suitable profit being, of course, largely dependent on the velocity of turn-over).

Note that this is a flexible clause, that it would win the confidence of labor, and that it places the emphasis on consumer-satisfaction by limiting not the amount of profit but only its rate of turn-over, velocity of turn-over being dependent on satisfied consumers.

Eighth, it would be impossible to exaggerate the historical importance of this bill if it became law. The scope of the bill is the equation of consumption to production, but the consequences of raising consumption to production are far-reaching. In particular, three gigantic problems of government are simplified and made susceptible of solution.

They are the problem of taxation, the problem of industrial disputes, and the problem of war.

The problem of taxation presents itself in this form: Government expenditures last year were approximately $9,000,000,000, but tax receipts were less than half that amount. It is impossible to raise the revenue needed by taxing the people in the higher-income brackets. It has been calculated by the economic journalist, Mr. John T. Flynn, that if every income above $25,000 a year were taxed 100 percent the Government would still be short. If you tax the rich heavily, in time there will be many fewer rich to tax. But the Government expenditures go on. It will be necessary to tax heavily all incomes, and already we hear the income-tax law must be changed to apply to every income, and the rates of taxation on every income must be steeply raised.

This means a groaning, unhappy, resentful population, an increase of ugly tension, finally a breaking point. The inevitable economic trends of our era are a rising curve of technological improvement, a rising curve of the permanently unemployed, a rising curve of Government expenditure, and a rising curve of taxation. These trends are related and will produce, unless an economic rectification takes place, a shattering explosion.

H. R. 7188, by immediately lifting the national income and by providing for national income to be increased as production mounts, immediately alleviates the taxation strain. It makes it easier to pay tax bills and to balance the Budget. It should be added that the full Douglas social credit scheme abolishes the unnecessary evil of taxation. On this point, as on several others, H. R. 7188 is highly conservative.

The second problem, industrial disputes, arises from the clash of interests of employers and employees in a situation of insufficient money. They are driven into a bitter wasteful struggle for power to redistribute the inadequate national income in the interest of one or another section of society. There is no solution—not in communism, not in fascism—to the struggle waged in these terms of money scarcity. The only possible solution lies in the credit-power of the Nation which is not now monetized. H. R. 7188 taps credit-power which now is not allowed to function, and this credit-power, pouring on to the scene of industrial strife and benefiting both sides, will promptly alleviate the struggle to redivide the short supply of money.

We live daily in the fearful shadow of the third problem, war. The slogan, poverty at home is the cause of war abroad, is terribly true. Practically all statesmen today are striving to remove unemployment at home, and they all know that the short cut to this is the capture of foreign markets, which incidentally are diminishing. The nation which loses foreign markets in this competition faces intensified unemployment and bankruptcy and is driven from economic warfare to military warfare. H. R. 7188 will produce very quickly a radical reduction of poverty and insecurity in our population. It will, for a time, give full employment, as business speeds up to meet the increased effective demand for consumers goods. By enabling the home population to claim a much larger proportion of the home production, it greatly relieves the pressure for foreign markets. It is a practical step toward setting our national economy in order, toward creating a prosperous, happy citizenry, toward the removal of our Nation from armed conflict over fields of foreign investment.

It is impossible to exaggerate the historical importance of the bill introduced by Mr. Goldsborough.

I would like to supplement this brief with a few remarks made from notes.

My first point was that the underlying tendency of the bill was reflected in advanced industrial and banking opinion. I take Mr. Henry Ford as an example of the aware industrialist; that is, an industrialist who knows what the aim of industry is, namely, to produce and deliver goods to consumers, and who is aware of the extent to which that aim has been frustrated.

Mr. Ford has been telling us for years that the banks have too much to do with the function which industry is trying to fulfill. As an example, in this country, there is not to the extent that there should be the advanced banking opinion which would be sympathetic with the aims of this bill.

I might mention the late Guy Mallon, eminent lawyer in Cincinnati, at one time a member of the Ohio Legislature, and for a number of years a bank president in Cincinnati. Mr. Mallon worked his way through to the truths of the new economics, and finally composed a book which was published a few years ago, called Bankers Versus Consumers. This title reflects, as I say, the opinion of a number of aware thinkers in industry and banking, who realize that the banking system today is somehow not adjusted to our increased productive capacity.

My second point was this: That the general field of ideas from which this bill is drawn, namely, the social credit ideas, must be sharply distinguished from mushroom economic cults. These ideas have been under fire for 20 years, and they are still advancing.

In my third section I gave the classic expression of the A plus B theorem. I would like to add a word here to that. The difference between a theory and a theorem is the difference between something which is speculative and something which makes an appeal to facts. A theory makes a statement, and draws a conclusion. A theorem is a proposition in mathematics, which states a conclusion and requires proof.

In the whole history of economics, I do not know of anything quite as audacious as the presentation of Douglas, not of a theory, but of a theorem, a statement that there is a chronic and inherent deficiency of purchasing power. This is a challenge, and it is a challenge made only by an appeal to facts. The only question is, Is it true or not? It is irrelevant to argue about a theorem. The relevant thing to do is to test it experimentally.

We say that the A plus B theorem has been proved a priori, a posteriori, inductively and deductively. We say that you can get experimental proof of it every week in any factory, and if you set a cost expert to work, it will be discovered that during that week the cost of the products manufactured for the market will be greater than the sums distributed to the employees. The cost expert will prove that it is impossible for the individuals receiving income payments from a factory at the end of the week to buy back the products made in that factory during that week. This has been presented to orthodox economists in the world during the last 20 years, and a great many of them remind me of the old lady who saw a giraffe for the first time and said, "I do not believe it." The orthodox economists have said, "I do not believe it," but they do something different from what the old lady did. The old lady did not go on to prove elaborately that such a creature as a giraffe could not possibly exist, which is what the orthodox economists have attempted.

Now, as I said before, a theorem has to do with rates, and rates are difficult for most of us to understand. Perhaps this illustration will clarify the matter. Let us consider the matter of births and deaths. Very well; every person who is born dies, and therefore the birth rate and the death rate are the same; therefore, population is stationary. We know of course that population is not stationary, that if the birth rate is faster than the death rate, the population increases, and vice versa. If the mortality rate is faster than the birth rate, population declines.

It is exactly the same case with this question of the rate at which costs are incurred in industry, and the rates at which incomes are distributed. We can say, if we like, with the orthodox economist, that every cost becomes income, and that therefore costs and incomes are equal, and that therefore there is no discrepancy between buying power and prices.

Well, we simply have to go back to this illustration of the birth rate and the death rate and say that as soon as you apply your minds to the question of rates, you can discover that the rates at which costs are piled up exceed the rates at which incomes are distributed to individuals.

My fourth point had to do with the necessity of our coming into consumption-finance. This necessity was recognized several years ago on the floor of the Senate by the late Senator Bronson Cutting, who made a speech in January 1934, so far as I know the first speech in American history on the floor of a legislature, declaring that the trend of the economic life was such that we must find some way of financing the consumer to do his part in our economic affairs.

Now, the consumer has a real title to this consumer credit. We must remember that credit is a joint creation; that it comes from producers and consumers together; that without consumers' productive ability does not amount to anything; and the bankers know that quite well. When bankers are considering the extension of a loan, they are interested in two things—the skill, ability, and resources of the producer. Has he the plant and workmen to make and deliver the product? That is one thing; and the other thing is this: Has he orders? Well, the consumers buy these goods, and that lets the consumer into the picture as being essential in our economic life. It makes him a joint creator of wealth. It gives him title to consumption credit.

In my fifth section, I declare that no cancelation provisions of a special type are necessary for the consumer credits which H. R. 7188 proposes to institute. Prices should be thought of as industrial debt. When you meet a price, you are meeting an industrial debt. At the present time, a portion only of the industrial debt can be met. Consumer credits are designed to meet the remaining portion. They are designed to cancel out those costs now incurred by industry, which we cannot meet with our income. We admit, scientifically, consumer credits into our economy. They appear at the retail counter. They go into the bank, and they face eventually producer debts, industrial debts, and when they do that, it is very much like a positive charge of electricity meeting a negative charge. What happens? These two forces neutralize each other, and vanish.

In the following section I speak of the national consumers' dividend, which is omitted from this bill, and I would like to point out here another justification for the dividend—an economic justification. We are all familiar with what is known as the problem of technological unemployment. We know that the purpose of labor-saving machinery is to save labor, is to displace men from industry, is to make them outcasts from industry. They are not wanted any more. A labor-displacing machine does fulfill its aim.

You cannot absorb those men expatriated from industry at the rate at which they are thrown out. It is perfectly true that you can absorb some of them. We can point to statistics from time to time and say that unemployment figures are down now, that there are new trades, new services, and that we are reabsorbing the unemployed. Nevertheless again it is a question of a rate, the rate at which they are being displaced from industry, which must be greater, thanks to modern invention and applied science, than the rate at which they can be reabsorbed into employment.

What are we going to do about these men who, through no fault of their own, are expatriated from industry?

Mr. **Patman.** Mr. Chairman, since the witness has evidently finished his discussion of this bill, I wonder if it would be in order for me to ask him a few questions.

Mr. **Hancock** (temporarily presiding). Does the gentleman care to yield now, or finish your supplementary statement?

Mr. **Munson.** I would prefer to finish my supplementary statement. At the beginning, the chairman agreed that I could, and it won't take very much longer.

Mr. **Patman.** I thought that you had finished your statement.

Mr. **Munson.** No. At the outset I asked if I might, after reading the statement, reinforce it with a few supplementary remarks.

The national dividend at least is a provision for taking care of men who will be permanently without jobs.

My seventh section raised the question of profit regulation, profit limitation. We must remember that such a proceedure as is outlined in this bill is a practical guaranty of profits to all efficient business men. Profits are not quite guaranteed, but the only reason under a social credit plan why profits cannot be made would be the fact that the businessman was trying to market an article that the people did not want. The consumer would say, "We do not want that," and the businessman carrying it would find himself forced out of business.

In consideration of this state of affairs, we say that it is perfectly reasonable to suggest that some sort of profit-regulation, profit-limitation clause should be incorporated in the legislation, bringing to pass that state of affairs.

My final point had to do with certain broad practical implications which could be drawn from this bill. At the present time, money is the master. A bill like this would make money the servant of society. At the present time, many things which are physical possibilities prove to be financially impossible. We know that while we live in a period of real wealth, we also experience financial poverty. What this bill does is to make a beginning toward a statement like this actualized: "What is physically possible should be financially possible."

Let us translate that into figures, and then try to visualize them. We know as the result of very careful research that in the year

1929 it was physically possible to supply to the American people consumers' goods and services at the rate of $135,000,000,000 for that year. We know that the income of the American people in that year was $81,000,000,000. You have there about $54,000,000,000 worth of consumers' goods and services which nobody got. Physically possible it was to provide these goods and services, but what was physically possible somehow proved to be financially impossible. Instead of a mirror reflecting this real productive capacity, a veil was thrown over $54,000,000,000 worth of it, and we could not see.

Now, supposing that you do set up a mirror, and H. R. 7188 will work out as a mirror of real productive and consumption facts in this country; then we will be able to tap this unmonetized credit power, and let us translate that into the kind of America that we would have; let us translate that into a rehousing program, so that all of our citizens could live in decent houses; let us translate that into terms of food, warmth, clothing, better looking citizenry, and a happier citizenry.

Think, finally, what it means in the field of education. Just as soon as you get a vivid impression of this picture of our real wealth, defined as what is physically possible for us to produce, and then translate that real wealth on the axiom that what is physically possible should be financially possible for us, you get a picture of what really would be a new American society.

Now, gentlemen, I will be very glad to answer, to the best of my ability, any questions that you may care to ask me.

Mr. Ford. Mr. Chairman——

Mr. Hancock. Mr. Ford.

Mr. Ford. Just one question occurs to me. You say that when consumption occurs in business, production takes care of it. That is all right, but isn't your assumption based on the proposition that every man has the earning capacity or the earning power or capacity to earn a sufficient amount to purchase all of the things that he needs and many of the things that he wants? All men have not got that earning power, have not got the physical capacity and the mental capacity in industry to make them worth a sufficient amount so that they get in wages from the industrial system the things not only that they need, but all that they want.

Mr. Munson. I agree completely with the point that you have raised. There would be inequality of earning power, but it is an inequality which on the whole we think desirable, as our system is designed to run on the inducement principle. We would like to have people very eager to make more and more money. Others, perhaps having other aims in life, would say, "I will be satisfied to get along and live frugally on a small amount of money," for such persons in a prosperous state can do that, and to us who want the national dividends to function, that would take them out of the industrial life where they are not needed, anyway.

But what we must think of is in terms of totals. The total buying power of the public should be equal to the total prices of goods and sales. Within this total of buying power in the hands of the public, there would be many differences in holdings, from much to nothing. Some, as at present, would have very little compared to others. But what we are aiming, first of all, is not to do anything about the maldistribution of purchasing power, but to do something about the total inadequate purchasing power. No matter how you redistribute purchasing power today, you cannot make an adequate purchasing power equal the total price.

Mr. **Ford**. Do I understand that in 1929, when we were at the peak of our consumptive ability and also at the peak of our productive ability, there was not sufficient purchasing power in the whole of the Nation to absorb the products? At that time, unquestionably, there were a lot of people that had much more than they needed to buy the things that they wanted and had to have, and others had so much less that there was an inequality of distribution, so that the result was a piling up of products. Now, there were probably 50 men in the country at that time who, if they had used all of their income to purchase things that they did not need, as against 5,000, 10,000, or 20,000 who did not have enough to purchase what they needed, we perhaps could have had an equalization. But, as a practical problem, we do not have it, because a man with an income of $20,000 a year does not purchase much more of what he normally needs than the man with an income of $10,000. He may have a few more servants, a little bigger place to live in, or maybe more motor cars, and all that, but he does not purchase to the extent of the amount of his income, whereas the man who gets $3,000 to $4,000 uses all of the money that he gets. The other man puts some of his money, over what he does expend, into investments, and I cannot quite grasp how we are going to supply, by financing consumption, that lack of earning power on the part of the great mass of the people.

You know, we had 22,000,000 people in the United States who were living, you might say, half on the subsistence line, which means that their earning power was just sufficient to let them get by, and that was supplemented in many cases by private charity. We did not know about that then, but one research specialist did develop that in a book, a man whose name I have forgotten, a German. But when the depression came on, that meant that 22,000,000 people who were unable to care for themselves were thrown on the Public Treasury, and then we discovered that we had them.

Now, any plan that would finance consumption for that mass and bring people up to a point where they could consume enough of the products of the country to put production and consumption on an even keel would of course solve the problem, but will it be solved by an interbank currency, and a 15-percent discount? I do not know. I would not say that it would not, but I would hesitate to say that it would.

Mr. **Munson**. Your question has touched on a field in which some extraordinary research was done under the encouragment of the United States Government. The year 1929 was taken, and a group of technicians were put to work to study the actual production of the year, the actual consumption, and the possible production and the desirable or budgeted consumption, and I do not believe that the fact can be disputed that even if the situation had not been aggravated by savings as it was in 1929—even if every dollar had been spent by the American people, it could not have claimed the possible or the desirable production of our country. You see, you have always this unused capacity to produce, for which no money exists to make a call upon. That goes back to 1921, when we first started collecting figures on that. I believe that the United States Government reported in 1921 that we were running at about 52 percent of our capacity. In 1923, speaking from memory, it was about 71 percent of our capacity. We get right on up to 1929, and it is expert engineering judgment, based on research, that we came nowhere near making a call on our productive capacity in 1929.

As you pointed out very well, in that same year an appalling percentage of our people were living in conditions of straitened circumstances, a great many of them below the health and decency line, a great many of them with families living on less than $2,000 a year. It is only a minority in this country who live decently. These people wanted in 1929 more goods and services, more comforts, and the money was not there to claim it.

Think of that figure, 135 billion dollars of capacity to produce goods and services, absolutely proved, and only 81 billions in 1929 to make a call on it. You have a difference there of 54 billion dollars worth of goods and services, with the factories ready, with the raw materials there, and with no bottlenecks in our productive system, with nothing to hold up the delivery of these extra goods except lack of money.

Mr. FORD. Lack of purchasing power.

Mr. TRANSUE. You stated the fact that the salaries or wages paid to the workers never equaled the price of the products that they manufactured. That was your statement, was it not?

Mr. MUNSON. Yes.

Mr. TRANSUE. Would that not always be so under any system? Would the capital investment be entitled to any earnings?

Mr. MUNSON. Yes. That is an extremely interesting question. You see, the A plus B theorem states that this discrepancy must exist. We accept that state of affairs. This bill accepts that state of affairs. It does not propose any kind of new industrial accountancy. It simply says, let us neutralize the effect of this discrepancy. We say that there is this difference in rates, and that the workmen cannot buy the products which they make, therefore we will neutralize that by admitting from another source debt-free money, money that does not leave a trail of cost behind it, in an amount sufficient to make up the difference.

Mr. TRANSUE. And that is this interbank currency?

Mr. MUNSON. The interbank currency notes are an administrative device to bring that about.

Mr. TRANSUE. Is that the device that you are going to do that with?

Mr. MUNSON. The central element is the national credit account, maintained at the office of the Secretary of the Treasury.

Mr. TRANSUE. This interbank currency, or whatever it is, is an obligation of the Government, is it not? When you drive it right back to its source, this interbank currency is an obligation of the United States Government, as proposed by this bill?

Mr. MUNSON. I would not put it that way.

Mr. TRANSUE. What is it?

Mr. MUNSON. It is an obligation of the American people.

Mr. TRANSUE. That is the same thing, is it not?

Mr. MUNSON. Not quite, because it is the American people who are represented by their Government who produce the wealth back of this money. The American people might fall down on their obligation; they might not produce the wealth to back it.

Mr. TRANSUE. Would that interbank currency keep piling up and piling up as the necessity demanded?

Mr. MUNSON. It could not. If I might put it this way, the interbank currency notes are a gadget. The essentials of the bill are the dispensation to the patrons in the retail shop of a discount.

Mr. TRANSUE. There must be some device to bring that about.

Mr. MUNSON. That is correct; yes.

Mr. TRANSUE. There always will be a discrepancy between the cost of the goods that are manufactured and the wages paid to the workers as long as you accept the theory that capital is entitled to some earnings.

Mr. MUNSON. Yes; that is right. Then you have your shopper getting the discount; that is an important thing to keep in mind. A person who sells to this shopper, a vendor, must be reimbursed. The national credit account should be debited for that. Now, the mechanism in between—and that is why I call it a gadget—is this device of the interbank currency notes. Think of that as a credit bridge between the Treasury, which is maintaining this national credit account, and the banks, who are marking up the deposits of retailers. It is a device of administration.

Mr. TRANSUE. But, when you get right down to it, the Treasury has to make good these interbank currency notes to the banks if it is called upon to do so, and it is still an obligation of the Government, is it not?

Mr. MUNSON. Where we are getting to is this: We are getting to the crucial question of who owns credit. At the present time, by custom, it is assumed that the banking system owns credit. Therefore, it is issued as a debt to the community. But it happens to be the credit of all of us. It happens to be our ability to produce real wealth, but when this ability of ours to produce real wealth is monetized, it is monetized in the form of a debt.

Now, in the case of the national credit account which it is proposed to set up in this bill, we get debt-free credit. It is assumed that the American people really own their credit, that they monetize it on behalf of themselves, and that they cancel their credit as they consume wealth. In other words, the backing of the national credit account, of which these interbank currency notes are a device, consists of goods and services. It is a physical backing. We, so to speak, issue tickets corresponding to these goods and services. As we use up these goods and services, our national credit account should show that. We are consuming real wealth.

So the simple principle of the bill is this: To issue money at a rate corresponding to what we can produce and to destroy money at a rate corresponding to our consumption or destruction of real wealth.

Now, then, you see, these are credits, and not debts, that we are talking about. The community is willing to accept goods in payment for the credit that it creates, and says, "Very well; we have created $10,000,000,000 of credit, and it is circulating in the form of these interbank notes. We have got the goods. We are paid off." But the banking system says, "Oh, no; we want money besides when we issue credit."

Mr. TRANSUE. But this is the point that I am asking about, that the bank will get this interbank currency, and then it will want its money and it will demand it from the Government, and it will get dollars that circulate for it, if I understand this bill. Is that your understanding?

In other words, if the bank has in hand this interbank currency issued to it because of this discount, and it is in need of circulating money which it has credited to the retailer because of this discount, then it is entitled to get that circulating money. Is that your understanding?

Mr. **Munson**. My understanding is that that is so in case of emergency.

Mr. **Transue**. That they are entitled under some circumstances to that money.

Mr. **Munson**. The bill does say that; yes.

Mr. **Transue**. That really makes it an obligation on the part of the Government to pay real money for this interbank currency, and makes it an obligation to pay 100 cents on the dollar for every dollar of interbank currency issued by the United States Government. Is that right?

Mr. **Munson**. I would say that that clause was put in the bill as a safety against bank runs, against emergencies. You see the result of that, assuming that such a thing happened, and may I say parenthetically that the banking system would be sounder under this bill than it is now, when it can be closed by Nation-wide runs.

Mr. **Hancock**. May I interrupt for this question?

Mr. **Transue**. Yes.

Mr. **Hancock**. If that is true, is it not a fact that under this bill the Government would become a copartner with every producer in the United States to the extent of the individual purchaser's needs and wants up to 15 percent?

Mr. **Munson**. Have you completed your question, sir?

Mr. **Hancock**. Yes.

Mr. **Munson**. I must have missed a word of that question. I must have missed the verb in it. I am sorry.

Mr. **Hancock**. If you admit that in certain cases the Government would have to refund or replace interbank currency with circulating currency, is it not a fact that under this bill the United States Government becomes a copartner with each purchaser or citizen to the extent of 15 percent of that purchaser's needs and wants?

Mr. **Munson**. Well, if I understand that question, to have meaning it would have to be something like the situation early in 1933, that is, a national emergency in the banking system, with hundreds of thousands of citizens calling at the banks for cash. Is it such a situation that you are visualizing or an isolated bank run?

Mr. **Hancock**. Well, I visualize that situation, but I am wondering if it is not a fact that under this bill the Government could, whether it would or not, become a copartner to the extent of 15 percent. I am not asserting that it necessarily would. I am seeking information.

Mr. **Munson**. Yes; I am trying to understand the question.

Mr. **Hancock**. Do we not in this bill say that there are certain conditions that may arise in the United States whereby the Government would join with the individual purchaser in supplying that purchaser with his needs and wants up to 15 percent?

Mr. **Munson**. Well, now, specifically, in this section of the bill, it seems to me that it is the Government coming to the aid of a bank which finds itself in temporary difficulties. The consumer and the retailer have already been fixed up. The national credit account is reflecting the moving facts of the situation. But let us say that there is a large bank in New York City which for some reason finds that it is hard pressed, finds itself in an emergency. I would say that that was more of a safety-insurance measure for the stability of the individual banks than it was a copartnership measure on the part of the Government.

Mr. **Transue**. You mean because it gives them an asset, a liquid asset, of whatever amount of interbank currency they have, that they can convert into cash upon demand on the Government?

Mr. **Munson**. I think that that would be correct to say.

Mr. **Transue**. And that this interbank currency is some time going to be retired, is it not?

Mr. **Munson**. I would not say so.

Mr. **Transue**. What is that?

Mr. **Munson**. I would not say so.

Mr. **Transue**. You do not think so?

Mr. **Munson**. No; I do not.

Mr. **Transue**. Where is it going to go? Is it going to stay stationary in the banks?

Mr. **Munson**. It will circulate in the banking system, and only in the banking system. You see, we have to think of the Government as bookkeeper for the Nation. That is why I balked a little at that word "copartner." The Government keeps the record of production and consumption. What has been done in this bill is to take the marvelous technique of bookkeeping, credit creation by the banking system, and using it on behalf of the people and through the Secretary of the Treasury, but, you see, there is the all-important difference between the people, through their bookkeeper, the Government, creating credits on their behalf which they own and which they credit to themselves, not as debts, but as something representing unmonetized wealth, and something which has to be redeemed at the present time, because it represents borrowed money. You see, there is no borrowing, no lending, in connection with the interbank currency notes.

Mr. **Transue**. That is all.

Mr. **Patman**. Mr. Munson——

Mr. **Goldsborough**. I believe that Mr. Luce is next.

Mr. **Luce**. We have developed in the last 20 years a huge system of credit known as installment buying. Theoretically, all who buy on the installment system have sooner or later to pay back all that they have borrowed. Do you think that that system has added anything net to the purchasing power of the community?

Mr. **Goldsborough**. You mean in the long run?

Mr. **Luce**. In the long run.

Mr. **Munson**. I would say not. I would say that it has merely shuffled up what purchasing power we have. You see, it is a desperate device to sell goods, for which at the present time the money does not exist.

Mr. **Luce**. It is in anticipation of future earnings.

Mr. **Munson**. That is correct.

Mr. **Luce**. Is it possible in any way to advance credit that must not be paid back?

Mr. **Munson**. Yes; it is, but not under the present system.

Mr. **Luce**. Is it possible under any system whatever?

Mr. **Munson**. It is, as provided in this bill, possible to do that, but it is not possible under orthodox economics, where the very condition of the entrance of money makes it a debt.

Mr. **Luce**. So the installment system is a debt, and you have admitted that there is no net income in purchasing power in the long run.

Mr. **Munson**. Well, you see, in the case of installment buying, the individual simply hopes from his future earnings to pay for the goods as the payments fall due. There is no special creation of money involved to finance him.

Mr. **Luce**. Money is simply the medium by which transactions are conducted.

Now, if it is true that all debts have sooner or later to be repaid. then a net gain to the community is hardly conceivable.

Mr. **Munson**. That is true. As a matter of fact, as you know, what we have is a piling up of debts, irrepayable debts, under the present system.

Mr. **Luce**. What are the irrepayable debts, as an instance?

Mr. **Munson**. I would say that a large part of our debt structure today is not repayable, cannot be paid.

Mr. **Goldsborough**. If you attempted to pay it, you would have a temporary inflation?

Mr. **Munson**. You would.

Mr. **Luce**. It would be simply repaying it from one hand to another. The wealth would still exist. It would not be enlarged nor diminished.

Mr. **Goldsborough**. Not the wealth, but the money that repays it.

Mr. **Munson**. The debt has been mounting up in a greater volume than wealth; and you have a great piling up of debt.

Mr. **Luce**. That is simply a transferring of legal title from one person to another. You have not increased or decreased the volume of production.

Mr. **Munson**. I grant you that debt and money in general have very little relation to production, to the physical things that we can do. You see, that is the point of our argument, that money and production are not geared together. This bill in its preamble, I believe, says that we want to establish a definite relationship between our supply of money and our domestic business and trade.

Mr. **Luce**. Going back to basic principles, I cannot follow you. But let me ask you another question.

You gave us to understand that the money in the hands of the people is not sufficient in volume to warrant their buying goods and thus increasing production. Let us take the example of a corporation which takes in $100,000 a year. We find that about two-thirds of that goes to labor, and of the other third, it goes into various subdivisions, but about 6 percent, as I recall it—and the figure is immaterial—goes to pay for capital investments and dividends. The remainder of that one-third goes into overhead charges. Would you question the fact that all of those overhead charges sooner or later go to pay labor?

For instance, take a newspaper. It has, besides its wage roll, its paper to pay for, its presses to buy, its rent to pay, its electric light, its insurance. Does not all of that money sooner or later go to labor, and, if not, where does it go?

Mr. **Munson**. Yes; it is perfectly true that practically all overhead at one time or another is distributed to individuals in the form of income, but the important phrase there is "at one time or another." What we are stressing is the time factor. We cannot buy goods now with money which was spent long ago and canceled, and yet we find in the prices of various articles ancient, dated costs for which money was once issued, money which has been spent and recalled, nor can we buy goods now with money allocated to reserve. Reserve has the effect of raising the price level without distributing out of it any purchasing power. Sure enough, some time later the reserve will be called on and spent, but we have to keep always in mind the question "now"—we have to take a line called "now," which is always moving from week to week through industry, and now we can say that the money in full is not available for meeting industrial debts as they are embodied in prices.

So it is true, as you have said, that we can think of these overheads as having been distributed to individuals, but they have been distributed over a period of time, and what we are concerned with is closing the gap between price and income at a given time. We are concerned with the availability of money to clear the market of any given day of the month.

Mr. **Luce**. My observation as an employer, one engaged in a business in which large quantities of paper are brought, is that a very rapid transit of the money that I get takes place from my checkbook back to the workers and to those who supply what I need.

Mr. **Munson**. Yes, and there is also a rapid transit of money when the paper is bought immediately by the consumer back to the banking system to be canceled, you see, starting with the paper factory——

Mr. **Goldsborough**. Mr. Luce does not admit that he has to borrow money.

Mr. **Luce**. I never borrow money.

Mr. **Munson**. It is an admirable practice, which the whole country cannot follow.

Mr. **Luce**. But that does not seem to affect the declaration or the idea that a worker or wage earner might be benefited if more money were put into circulation. I do not think that that is valid.

But I have one more question. Where, in principle, does this proposal differ from the Townsend plan, which contemplates from an economic point of view the furnishing of money to people to spend for consumer goods?

Mr. **Munson**. Well, I should say that it differed in every possible respect.

Mr. **Luce**. I am talking about principle. The Townsend people proposed that we shall pay over money to the aged, in order that they may spend it. Where does this proposal, in basic general principles, differ from that?

Mr. **Munson**. In this, that the cardinal feature of the Townsend plan was to raise this money by taxation. This bill does not raise the consumer credits by taxation. This bill creates fresh purchasing power, instead of trying to derive it from purchasing power already existing and distributing it to a section of society. In other words, under the Townsend plan the rest of us are going to pay for the money which the aged people will receive, but the total income would not have been increased.

Mr. Luce. But their purpose, they say, is that if you pay the money to the aged, they will spend it immediately, that we will require them to spend it immediately in order to increase production.

Mr. Munson. It is a simple fallacy in economics that velocity of circulation will increase purchasing power, but no matter how much the money spins around, the amount does not increase, and yet Dr. Townsend and his friends feel that if you spend this money fast enough, it will be greater in amount than it was. There is no creation of fresh purchasing power under the Townsend plan, and from our point of view it is utterly fallacious.

Mr. Ford. There would be in a group; you would be transferring purchasing power from all of the people to one group.

Mr. Munson. That is right; it would be a redistribution of purchasing power.

Understand me, I think the aim, the vision of the Townsend movement was good. It is a vision shared by many movements today, and we have not yet heard the last of them, and will not until something is done to rectify our money system, but in the case of the Townsend movement there was a vision, a groping for some means to actualize itself, and the groping was, from the point of view of an economist, very silly.

Mr. Luce. But where does it differ from this proposal, which contemplates putting into the hands of the consumers of the country additional purchasing power?

Mr. Munson. The difference is that whereas the Townsend movement relied upon a transaction tax—it relied upon taxation to finance its scheme, this bill does not rely upon taxation or upon any part of our existing income distributed as it is nowadays to bring into existence consumer credits, new purchasing power. This bill adds to purchasing power, debt-free buying power of the American people, coming in on the consuming side, without debt attached to it, without relying on taxes to raise it. It is new money entering into our economic life, not, I repeat, as debt, but as a credit to the American people, to be destroyed as we consume the goods which it represents.

Mr. Luce. That is all.

Mr. Spence. I see no mandatory provision in the bill requiring the banks to come under the provisions of this act. Is that to be a voluntary act upon the part of the bank?

Mr. Munson. That is a question which I think the drafter of the bill could answer better than I can, I would say. The reason that I hesitate is that I am not familiar with the legal phraseology in the question.

Mr. Spence. What bothers me about it is that, as I understand it, this 15-percent credit is not segregated in any way. It is placed to the credit of the consumer, and he can draw on it when he pleases.

Mr. Goldsborough. You mean, the retailer can?

Mr. Munson. That is right.

Mr. Spence. And it is as much a credit to him as any other part of his deposits in the bank. He has actual control over that?

Mr. Munson. That is absolutely right.

Mr. Spence. Which a bank cannot change at all by any act of its officers? Is that true?

Mr. Munson. That is right.

Mr. Spence. It is a vested interest.

Now, there is a provision in the law reading:

> Upon the findings and advice of the Federal Credit Commission indicating that inflationary conditions are tending to arise, the Secretary of the Treasury is hereby authorized and instructed to recall from the banks such amounts of the interbank currency in their hands as may be necessary to establish and maintain monetary equilibrium.

That interbank currency represents this credit which has been given to the retailers. If the National Government now recalls that without returning to the banks lawful money, what is going to happen to the banks? That is what I want to know.

Mr. Munson. Accurately, the interbank currency notes are sort of a warrant for the banks to mark up their depositors' accounts to the extent of the discount provided.

Now, my view, which evidently is not the view of the drafters of the bill, because they put this provision in there—my view is that such a clause could never become active. My brief was devoted in part to proving that an inflationary condition could not possibly arise.

Mr. Goldsborough. Nor a deflationary condition?

Mr. Munson. Nor a deflationary condition. So, from the technical point of view, this particular section which you have read is unnecessary. From a psychological point of view it may be necessary, but technically it is not necessary.

But now, supposing that this did happen; supposing that some of this money was recalled. It would simply mean that there would be less money available in the country, exactly as happens now.

Mr. Spence. But from a practical point of view, the bank would lose the 15 percent, would it not?

Mr. Munson. No; a bank would not. Where that 15 percent has been lost is in the national credit account in Washington. It has been lost through consumption.

Mr. Spence. But what happens to the bank if it extended this credit to the patrons of the bank, and has lost it? Why would a bank voluntarily come in under a scheme like this, and subject itself to a loss of this kind, when the bank that stayed outside would not be subjected to that loss?

Mr. Munson. I do not see what the bank has lost. You start with your deposits made by your retailers, which are marked up. Intermediate between the national credit account at Washington and your ordinary customers' accounts at the bank, you have an interbank currency notes account. This is charged when the customers' accounts are marked up. It is put in balance when the interbank notes are received from, I suppose, the Federal Reserve bank of that district, from the Secretary of the Treasury. That account is in balance, and it is in continuous balance, and there is the general ledger deposit account in balance with your customers' accounts. Now, that goes along continuously from day to day.

Mr. Patman. I would like to ask the gentleman some questions.

Mr. Goldsborough. Very well.

Mr. **Patman**. But before I do, will the chairman tell me what he has in mind for the committee for the rest of the week?

Mr. **Goldsborough**. As far as I know, Mr. Munson has not finished, and Mr. Crawford has several questions, and Mr. Harvey will go on tomorrow, and after he finishes, I would like the permission of the committee to answer various issues which have been raised.

Mr. **Patman**. You mean yourself?

Mr. **Goldsborough**. Yes.

Mr. **Patman**. And that will be the close of the hearings, then?

Mr. **Goldsborough**. No.

Mr. **Patman**. Since 160 of us are sponsoring this other bill that it coming up for hearing, some of us would like to know when we may be expected to appear and testify. Would next week sometime be all right?

Mr. **Goldsborough**. I do not know.

Mr. **Luce**. May I ask the chairman if he has any views as yet as to what other bills we are to hear?

Mr. **Goldsborough**. Mr. Steagall did not know the last time we talked to him.

Mr. **Patman**. Well, there will be tomorrow, and the Chairman expects to finish the day after tomorrow?

Mr. **Goldsborough**. Well, I am not sure about that.

Mr. **Patman**. As far as you are concerned, would it be all right to start on our bill next week?

Mr. **Goldsborough**. We have not tapped these hearings yet, Mr. Patman. We are here attempting to work out a problem. This bill may not do it as it now reads, but we hope—or I hope at least—that it will serve as a model, and the hearings are certainly not completed by any means. A great many bankers want to be heard, and there are sections of the executive departments that want to be heard, and there are wholesale and retail organizations and farm organizations that want to be heard.

Mr. **Patman**. You mean in support of this bill?

Mr. **Goldsborough**. Well, on the bill, either for it or opposed to it.

Mr. **Luce**. If the housing bill is to come before us, there is no probability of finishing on this bill at this session.

(At this point there was a call of the members to the floor of the House.)

Mr. **Goldsborough**. We will have to adjourn until tomorrow morning at half-past 10. I do not know whether Mr. Munson can be here or not.

Mr. **Patman**. I would like to ask him some questions. I hope that he can be.

Mr. **Munson**. I am sorry. I cannot be here tomorrow. I would like very much to hear the questions now.

Mr. **Patman**. It would not take me over 5 or 10 minutes, if you won't expand your answers.

Mr. **Goldsborough**. I think that it is only fair to the witness that he should be able fully to answer the questions.

Mr. **Munson**. I would be perfectly willing to give as brief answers as possible.

Mr. PATMAN. This is really part of the Douglas plan, is it not?

Mr. MUNSON. I would say that it is derived from the Douglas plan.

Mr. PATMAN. It is derived from the Douglas plan, and the only essential part of the Douglas plan that is left out is the national dividend part, is it not?

Mr. GOLDSBOROUGH. You are expressing your opinion, of course?

Mr. MUNSON. I am expressing my opinion on that, and that is in response to the previous question.

Mr. PATMAN. Yes.

Mr. MUNSON. You understand that I spoke here as a Douglasite.

Mr. PATMAN. That is right. You represent the Douglas theory?

Mr. MUNSON. That is right.

Mr. PATMAN. Are you the Douglas plan representative in America?

Mr. MUNSON. There is no official American representative.

Mr. PATMAN. But you consider that you are the spokesman for the Major Douglas plan?

Mr. MUNSON. I have been the journalistic spokesman for it.

Mr. PATMAN. As Major Douglas frankly says that it is for the purpose of lowering prices, the amount of the discount, say 15 percent, is to lower prices 15 percent, is it not?

Mr. MUNSON. It is for the purpose of increasing purchasing power, and——

Mr. PATMAN (interposing). At the same time it results in decreasing prices 15 percent?

Mr. MUNSON. Reduced prices are——

Mr. PATMAN (interposing). You said awhile ago——

Mr. GOLDSBOROUGH (interposing). You always break in on the witness before he finishes his answer.

Mr. MUNSON. Reduced prices are a means of increasing purchasing power. The emphasis should be put on increasing the purchasing power.

Mr. PATMAN. I know that you emphasize that, increased purchasing power, but at the same time that results in a reduction in prices of 15 percent?

Mr. GOLDSBOROUGH. Just a minute.

Mr. PATMAN. You conscientiously believe——

Mr. GOLDSBOROUGH (interposing). Just a minute.

Mr. PATMAN (continuing). That a reduction in prices will help this country?

Mr. MUNSON. It will help the consumer.

Mr. PATMAN. You stated awhile ago——

Mr. GOLDSBOROUGH (interposing). Just a minute, because I would like to have the witness finish his answers. I do not want this record in such shape that it does not show what the witness means.

Mr. PATMAN. I presume that the witness is the best judge of what he means.

Mr. GOLDSBOROUGH. I understand, but there is a persistent effort to stop him and confuse him. This will reduce the price to the consumer, will it not?

Mr. MUNSON. Yes, sir.

Mr. GOLDSBOROUGH. There is nothing in this bill which reduces the price to the wholesaler, the manufacturer, the retailer, or anybody except the consumer?

Mr. Munson. That is right.

Mr. Goldsborough. Make that clear.

Mr. Patman. And you are ready to say that a reduction by the retailer will not result in a reduction to the wholesaler, a reduction to the farmer, and everyone else?

Mr. Munson. There is no provision for any discount back of the retail counter.

Mr. Patman. If that is your opinion, you can keep your opinion; you are entitled to it. But, I say, is it not a fact that when you reduce the retailer, you reduce the others in proportion, just like when I go to town to sell eggs, and I am not a retailer, you will make me cut my price 15 percent, because you can go to a retail store and get a 15-percent reduction?

Mr. Munson. No; it does not work that way at all.

Mr. Patman. You would not pay me full price when you could get a 15-percent reduction from the retailer.

Mr. Munson. If you are a manufacturer——

Mr. Patman (interposing). But I am talking about the retailer, and I am selling eggs to you, or want to. You can buy the same eggs from the retailer at a 15-percent reduction, and you would make me take a 15-percent reduction or you would not buy from me.

Mr. Munson. If I understand your question, it is something like this, that under this bill the retailer may apply to the Government for a license to dispense the retail price discount. A retailer might not wish to do that. That would be his business. He might say, "I think I can do perfectly well without dispensing the retail price discount." He would go on, then, in the old way. But he would be competing with people providing just as good goods and services at the discount rate, so there would be no reason why he should not sign up and say, "I want a contract to dispense the retail price discount," in which case he is competing on equal terms with other retailers.

Mr. Patman. He could not stay in business in any other way, could he?

Mr. Munson. I might say that he would be under a great handicap.

Mr. Patman. The same as a farmer would be under a handicap, or others who sell directly to the consumer. If they have not a retailer's license, they could not compete.

Mr. Munson. But they could get it very easily.

Mr. Patman. A farmer could?

Mr. Munson. Of course.

Mr. Patman. Anybody could get a retailer's license?

Mr. Munson. Anyone doing a retailer's business.

Mr. Goldsborough. There is nothing in this bill which would prevent him from getting a license.

Mr. Patman. But he would have to do a retail business in order to get his license.

Mr. Goldsborough. He is now doing it.

Mr. Patman. And the farmer could get it the same as anyone else?

Mr. Munson. If he is selling on a retail basis.

Mr. Patman. If he is selling eggs, trucking supplies, and so forth, he is doing a retail business, is he not?

Mr. Munson. Well——

Mr. Patman (interposing). There is another question. You said awhile ago that an amendment should be proposed to this bill which would protect the people against unfair prices and against the manufacturer's costs. You said that it was a system of guaranteed profits. What did you mean by that phrase, a system of guaranteed profits?

Mr. **Munson**. I said, as a matter of fact, practically guaranteed, and I might say this, that if you give the public sufficient money with which to claim its total products, you guarantee practically the profit. You do not absolutely, because, as I explained, the public might not want your product. Your product might be inferior, or might be too special, or might be antiquated, and you could fail in business just as well, but you would not fail as a great many businesses fail now because the public was short of buying power.

(At this time there was a second call for the Members to be on the floor.)

Mr. **Goldsborough**. The committee will adjourn until tomorrow morning at half past 10.

(Thereupon, at 12:15 p. m., an adjournment was taken until Thursday morning, July 29, 1937, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, JULY 29, 1937

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed the hearings on H. R. 7188 at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members present: Messrs. Goldsborough, Reilly, Hancock, Williams, Spence, Ford, Brown, Patman, McKeough, Evans, Transue, McGranery, Luce, and Crawford.

The **Chairman**. The committee will be in order. Who is to appear next?

Mr. **Goldsborough**. Mr. Harvey wants to answer a question that Mr. Patman asked him, and that he did not have a chance to answer. When he gets through, there is a lady here that wants to be heard.

The **Chairman**. Mr. Harvey, come around, please.

STATEMENT OF EDWARD F. HARVEY, OF GWYNEDD VALLEY, PA.—Resumed

Mr. **Harvey**. I hope that I won't take up much of your time.

Mr. **Goldsborough**. Have you the question in mind?

Mr. **Harvey**. Yes; and I would be glad to cover it.

Mr. **Goldsborough**. If it is satisfactory to Mr. Patman.

Mr. **Harvey**. Mr. Patman expressed the opinion that the intent or effect of this bill would be lowering the general level of prices. I cannot agree with that statement.

The purpose is to lower the prices of goods sold at retail, without affecting the general trend of prices of all commodities. The effect of the discount on prices at retail would be to increase demand and this would naturally tend to increase the general price level, which is advisable.

The impact of competition would be the governing factor of the general price level, as it is now. Retail prices would tend to rise, but the discount would offset this rise in relation to the general price level as far as the cost of living is concerned. Thus we would have a general "firming" of the price level. There would be more employment and a larger pay roll, which would further increase the demand for consumption goods.

This would be of immense benefit to general farming, because the farmer would buy his necessities and comforts at the lower retail price, while he would receive the higher ruling price for his products. He would thus benefit both going and coming.

As to the ability of the truck farmers to sell their products direct to consumers, my own experience is that farmers who do this follow one of two courses. They either make a specialty of certain choice products and sell them regularly direct to consumers at a price higher than that ruling for standard products in the store, or else they offer their surplus to their customers at lower prices than prevail in the stores. Convenience of deliveries and the freshness of the articles sold make them desirable to the purchasers.

If one bases a forecast of the general trend of prices under the proposed enactment, and on previous experience, it may reasonably be assumed that the general price level would rise to about the average of 1924–29, and would become stabilized there.

The reason for this is that in those years there was very free buying of commodities based upon a great expansion of credits, inflated monetary profits which arose from the rise in security prices and purchasing upon installments. These, together with the large pay rolls for production, offset the money withdrawn as savings and we had something approaching equilibrium in the industrial field, at a point about 20 percent below full industrial capacity.

This equilibrium was reached because the reduction in cost due to large volume production left a comfortable, even liberal margin of profits, and competition prevented prices and profits from being unreasonably kited.

The same thing might be expected to happen again under this bill, but the purchasing power that would generate it would not be of the unstable character that led to the end of that period, because it will be based on a monetary system not subject to sudden shrinkage and a credit system under better control.

But it will be the responsibility of the Federal Reserve Board and the Securities and Exchange Commission to prevent an inflation of securities and capitalizations which would again cause widespread financial trouble, if carried too far.

That is the way I interpret, from experience, how the farmers——

Mr. **Patman**. May I ask him——

Mr. **Goldsborough**. Wait until he finishes.

Mr. **Harvey**. The farmers will benefit in a number of different ways. For instance, we have heard a good deal about diversified farming. I think it is generally believed that diversified farming is the best farming. The one-crop man of the West and the South is always at a terrific disadvantage, and also the price of his products is governed very largely by the export markets. He is growing export goods to a very large extent. But, in diversified farming, it is the dairy man and the truck farmer who would benefit. We know perfectly well—and it is of record—that there is a tremendous shortage of milk in this country. The children are not getting the milk that they ought to get to make for full growth, and that, I think, is a matter of absolute record. The diversified farmer would have an opportunity of increasing his sales of milk, and the same thing, I think, applies to fresh vegetables and fruits.

I think that the people, when they found that their $100 a month or whatever it might be that they had, could buy $15 or $20 more, would appreciate the improvement in their well-being.

I may be wrong about it, but it seems to me that the farmer has a vital interest in this, the farmers would get it going and coming, as

I said before, because they would have a stronger demand for their products, and they would share with everybody else in lower prices for the purchases that they had to make at retail.

Mr. Patman. Now, Mr. Harvey, I asked you the other day about the number of establishments that would be involved, and since that time I have had the Bureau of the Census working in it. I gave the information to the Census Bureau about the retail establishments that I wanted the number of in the United States, and I have the figure here. They aggregated 2,866,349 retail establishments in America that would be involved.

Mr. Chairman, I would like to insert this table in the record.

Mr. Goldsborough. Certainly.

(The table referred to is as follows:)

Recapitulation showing number of retail stores and other establishments rendering services to the ultimate consumer (1937)

	Number
Total service establishments (see table 1)	573, 764
Total retail stores (see table 1A)	1, 653, 961
Heating and plumbing contractors [1]	23, 856
Theaters, including legitimate stage and opera	12, 182
Hotels	28, 822
Total for the United States	2, 292, 585

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[1] More than 50 percent of revenue from contract work. These do not duplicate the heating and plumbing equipment dealers shown under retail trade.

Table I.—*Establishments rendering services to the ultimate consumer*

		Number
Total for the United States		573, 764
Barber shops	121, 153	
Barber and beauty shops	4, 302	
Baths and masseurs' establishments (turkish, etc.)	1, 126	
Beauty parlors	61, 355	
Cleaning, dyeing, pressing, alteration, and repair shops	57, 397	
Funeral directors, embalmers, and crematories	17, 144	
Fur repair and storage shops	2, 113	
Laundries (not including power laundries)	16, 826	
Photographic studios	10, 402	
Rug cleaning and repairing shops	894	
Shoe repair shops and shoe shine parlors (including hat cleaning)	61, 046	
Other personal services	2, 218	
		355, 976
Business services:		
Disinfecting and exterminating service	596	
Linen, coat, apron, and overall supply service	619	
Photo-finishing laboratories	1, 002	
Sign-painting shops	5, 035	
Ticket agents and brokers	939	
Title and abstract companies	2, 042	
Window-cleaning service	749	
		10, 982
Automotive repairs and services		26, 228
Other repair services (except apparel and shoes)		60, 186
Custom industries		60, 518
Miscellaneous services		5, 949
Real estate and insurance and real-estate offices		36, 137
Motorbus transportation		1, 751
Tourist camps		9, 848
Hospitals (A. M. A. list for 1936)		6, 189

The bill grants any seller of goods the right to obtain a license. This will include all farmers, stock growers, and others, including millions of people, also such agents as Fuller Brush, Real Silk Hosiery, and others.

At least 10 or 15 million people may be licensed under this bill. Can the farmer get a retail license and sell hardware, drugs, and automobiles and give the discount? One thing is certain, all these millions of people will be privileged to make sales and give a 15-percent discount. Then take the evidence of the 15-percent discount to the nearest bank and obtain credit or currency for it. Then the bank will obtain interbank currency for it. The interbank currency is an obligation of the Government. Therefore millions of people will have considerable power to draw unlimited amounts of money from their Government through these sales.

Mr. PATMAN. Now, in regard to your 15 percent and the farmers, you said that the farmers should have a select product, a better product, and therefore get an increased price.

Mr. HARVEY. I did not know that I said that.

Mr. GOLDSBOROUGH. He did not say that.

Mr. PATMAN. Well, let us see——

Mr. HARVEY. No, I did not say that.

Mr. PATMAN. Did you not say that they would either have to have a select commodity, or——

Mr. HARVEY (interposing). I said that the general custom is now, and I know a number of farmers do it, to——

Mr. PATMAN. I wrote down what you said here, so I just did not understand it. I understood you to say that the farmer could do one of two things, either have a better product to enable him to have a better price, or accept a lower price for what he sold. Did you say that or not?

Mr. HARVEY. No, I said something else.

Mr. PATMAN. I am sorry.

Mr. HARVEY. I referred to what he had been doing, not to what he would do, but I do not see that there is any necessity for a change. He is very apt to do it that way, for his price is greater.

Mr. PATMAN. I know, but what he sells is in direct competition with the things that are sold at the store, and if the customer can go to the store and buy at a 15-percent discount, because that store has a license, the consumer, instead of buying from the farmer and paying the full price, will go to the retailer who has a license.

Mr. HARVEY. No, sir, I do not agree with you, because——

Mr. PATMAN. If you do not agree with that——

Mr. GOLDSBOROUGH. Let him finish.

Mr. PATMAN. If he has an explanation for it, all right.

Mr. HARVEY. My explanation is that the custom will continue as it is, and that the prices that they get from their personal customers, the farmers' personal customers, will be the same as they always have got.

Mr. PATMAN. And they would not quit and go to the store?

Mr. HARVEY. If they did make a slight reduction in price for the cheese and the eggs that they sell, I do not think that they would be very much hurt, but I am certain that the men who sell special goods, who make a specialty of butter, who make a specialty of eggs, or who make a specialty of certain fresh vegetables, will continue to get a higher price than the same things or similar things would be sold for in the store.

Mr. GOLDSBOROUGH. Right at that point, in order to settle it, because I want to find out what the answer is, is there anything in this bill which would preclude a farmer who was in the habit of delivering milk or eggs to a retail customer from getting a license from the Federal Credit Commission, in order to give him the benefit of this discount?

Mr. Harvey. No, sir, because he would have the right to say, "I am a milk distributor, and I would like to be put on the record, because I propose to allow my customers the discount, and will want to be reimbursed."

Mr. Patman. Let me ask the chairman a question. Are you in favor of the farmers being licensed that way?

Mr. Goldsborough. Of course, if they are doing a retail business.

Mr. Patman. That includes the Fuller Brush people? Would you license them?

Mr. Goldsborough. What do you mean?

Mr. Patman. They sell from door to door to consumers, as does the Real Silk Hosiery Co.

Mr. Goldsborough. I do not know. Of course, everyone in this room, unless it is you, knows that the farmer is not primarily a retailer. Why you insist that he is and merely confuse the issue is for you to decide; but, I say, everybody in this room except yourself knows that the farmer is not primarily a retailer, but a wholesaler.

Mr. Ford. May I comment on that?

Take the apartment house in which I live. A woman comes around there 2 or 3 days a week with eggs and butter and cheese, and one or two other products. The people in that apartment who deal with her probably each buy 60 cents worth. They would not go down to the store or pay 5 or 10 cents to telephone to the store to get the same thing, because she brings it to the door and they do not have to leave the apartment. That is a convenience, that has no relation whatever to the broad commercial principles that motivate the entire commerce of the country; and when I say this, I am not saying to the committee that I am in favor of this bill, but I am just arguing that one phase of it.

I know back home that we have people that come around and deliver oranges in buckets. We will buy a bucket of nice oranges for 15 cents, whereas if you went down to the corner store and bought them, they would probably cost you a quarter. But, on the other hand, they come around with first-class oranges that will cost you 35 cents, and maybe if you went to the store those would only cost you 25 cents, but still you buy them because they are fresh and you buy them for their quality. So the thing works both ways.

Mr. Patman. With that understanding, Mr. Harvey, and I notice that the chairman is right, because any seller of goods may be licensed; therefore any of the six and a half million farmers, or all of them, could be licensed, and all of the Fuller Brush agents and all of the Real Silk hosiery agents and all of the refrigerator agents, and all sellers of radios and different equipment direct to the consumers, could be licensed, and each one of them would carry a book along, and when he sold something he would have this customer, I presume, sign for it, or else he would sign for the customer, and then he would rush to the nearest bank and get that cashed or his 15 percent, wouldn't he? That would be about ten or fifteen million people carrying what will be called a checkbook on Uncle Sam around with them?

Mr. HARVEY. Well, sir, I do not know. As a businessman, if I tried to run that business that way, apart from any question of discount, how long would I last? My overhead would be so big. The Fuller Brush people have an organization, you know, and they would make their collections of discount for the goods that they sold at retail directly through their own banking facilities. Their agents would not have anything to do with that.

Mr. PATMAN. They would just turn them into the company, and get credit?

Mr. HARVEY. Yes.

Mr. PATMAN. But the company would get this credit of 15 percent?

Mr. HARVEY. Yes.

Mr. PATMAN. Have you considered the fact that the store would say, "I am putting on extra help to look after the paper work for the Government, and I have to take some of that 15 percent back," and the bankers would say, "This involves a lot of extra help for paper work, and I will take part of this 15 percent for the bank," and then, with the uncertainty of the value of the interbank currency, I am afraid that this 15 percent would not be enough, Mr. Harvey.

That is all.

Mr. HARVEY. That is entirely up to the Credit Commission.

Mr. PATMAN. They could make it more?

Mr. HARVEY. They can make it more or less.

Mr. PATMAN. Firty percent, if they wanted to?

Mr. HARVEY. Yes.

Mr. PATMAN. And let these ten, eleven, or twelve million people who were licensed to go to the bank and draw that?

Mr. HARVEY. Yes, sir; if they could take the cash in that would warrant that, and show their sales. Of course, in the case of any good-sized store, that would be tabulated and totaled; they would not take in all of the individual vouchers.

Mr. PATMAN. I see. Now——

Mr. HARVEY. That is a matter of commercial organization. I do not know what experience you have had in it, but, my gracious, look at the telephone bills, and look at all of this line of business that we are doing in this country now.

Mr. PATMAN. Yes; but there is 1 head to that, but here you have about 15 million heads, because every fellow would be a separate and distinct entity from all other retailers, and you would not require the farmers to carry one of these cash registers around with them that you referred to the other day; he would have to have some kind of memorandum in writing, and therefore there would be lots of people who would have a right to draw this money from the Government.

Mr. FORD. Assuming that 60 days after the discount had been declared in force by the Commission, their researches showed that production and consumption had come into balance; what would happen then? Would the discount be discontinued?

Mr. HARVEY. It would be discontinued. If one visualizes the way that it would work, it would probably gradually discontinue, because the growth of consumption would begin gradually and reach the productive capacity by less 15 percent, and we might expect in the second quarter, say, to have a 10-percent discount, and in the third quarter, a 5-percent discount. But, of course, one cannot foresee how that will work.

Mr. Ford. The American people are inclined to be "rush" buyers. A store sends out a page advertisement saying that it is going to sell a certain type of luggage this week at a 15-percent discount, and the chances are that the people will break their necks to get there, and it is probable that when a sudden national discount of 15 percent is declared on goods, practically everybody that needs those goods, thinking that it may be only a temporary matter, would rush to the stores and purchase them, so that within 60 days the disparity between consumption and production might be leveled off, and then the duty of the Commission would be, after it has put its statistical machinery into operation, to cut that discount off and let things go on the level until there was a movement up or down either way?

Mr. Harvey. Exactly.

Mr. Ford. Suppose that consumption began to go beyond production; what would happen?

Mr. Harvey. The first thing to do would be to reduce the amount of money in circulation. That would tend to decrease buying power.

Mr. Ford. Produce what?

Mr. Harvey. Reduce—reduce the amount of money in circulation.

Mr. Ford. In other words, to tighten up on credit?

Mr. Harvey. To tighten up on credit. That is what is done today.

Mr. Ford. Then this is really an instrumentality designed to push the string—I think that is the phrase that was used—and the Federal Reserve is the instrumentality to pull the string, to tighten it up?

Mr. Harvey. In that case, yes.

Mr. Ford. Does that express the philosophy of the bill in your judgment, Mr. Goldsborough?

Mr. Harvey. Of course, the public is pulling the string, and the Federal Reserve, or whoever tightens the string, would pull a little bit stronger than the public would pull, because the public is not a coordinated credit bureau.

Mr. Ford. I realize that, but it amounts to the same thing, in my judgment.

Mr. Crawford. Will Mr. Ford yield?

Mr. Ford. Yes.

Mr. Crawford. I want to get one thing clear, because I may be confused, whereas I think that you are.

As I understand this, when this act becomes effective, 15 percent governs until the Commission issues an order, we will say, and at that time the Commission has a 15-percent tolerance, and if production is not 15 percent above consumption, the Commission does not issue any order at all. Is that right, Mr. Chairman?

Mr. Goldsborough. That is right.

Mr. Crawford. Now, if the Commission finds production is 25 percent above consumption, in that case it would issue a 10-percent discount order. If next month it was 40 percent different, it could only move up 5 percent per month—is that right—so that there might be a difference of 15 percent of excess production over consumption and no discount in operation at all?

Mr. **Reilly**. There has got to be that difference before you can get this.

Mr. **Ford**. This bill does not say that.

Mr. **Goldsborough**. Oh, yes; it does.

Mr. **Crawford**. They can make this calculation only if there is 15-percent difference or more. If there is 15 percent or less, the interbank currency does not issue at all, and there is no retail discount.

Mr. **Ford**. Supposing it is found, after 60 days, that the discrepancy is 10 percent and the 15 percent is operating now?

Mr. **Goldsborough**. They would suspend the discount altogether.

Mr. **Crawford**. In other words, when the law became effective, the 15 percent would become effective until the Commission begins to function, and if on the date that the Commission begins to function it is only 15 percent, then no discount becomes operative?

Mr. **Ford**. The discount is discontinued.

Mr. **Reilly**. The discount starts at 15 percent, until the Commission finds there is no 15-percent difference.

Mr. **Crawford**. Yes.

Now, Mr. Harvey—I beg your pardon; I do not have the floor.

Mr. **Ford**. What I was trying to get cleared up in my mind is this: We will assume that the bill goes into effect today, and it will take the Commission, say, 60 days to determine what exactly is the difference between production and consumption. We will assume that in 60 days from now they will discover that the exact difference between consumption and production is that there is 25 percent more goods being produced than consumed. So they say, "All right; there is 25 percent difference, and we will raise this discount to 20 percent." Then in 60 days more, they find that consumption and production are about balanced. Then they discontinue the discount, or the 10 percent has disappeared, and there is only 15 percent. But in either case they would discontinue the discount, would they not?

Mr. **Harvey**. Yes.

Mr. **Williams**. Mr. Harvey, you have made a very careful and very thorough study of this question, and examined the statistics, I take it. What is the difference now between productive capacity and consumption?

Mr. **Harvey**. Assuming that productive capacity has not been increased since 1929—and I believe myself that it has been considerably increased——

Mr. **Williams**. You say, since 1929?

Mr. **Harvey**. I say, assuming that the productive capacity of the country is the same as it was in 1929, and taking the figures of the Brookings Institution and the figures of the other Government agencies, and splitting the difference, there would now be about a 30-percent shortage of consumption as against the productive capacity.

Mr. **Goldsborough**. And that is why the 15-percent discount was fixed in the bill?

Mr. **Harvey**. That is the reason for the 15 percent in the bill, that the 15-percent margin of safety was fixed in the bill.

Mr. **Williams**. Do I understand that it is the intention of this bill that, in case the Commission finds, after this bill goes into effect, that there is a 30-percent unused productive capacity, the discount rate will be 15 percent then, or will it be 30 percent?

Mr. Harvey. The discount rate then will be 15 percent, presumably.

Mr. Williams. You will have a leeway of 15 percent all the time? You are to assume at all times that difference between consumption and production of 15 percent in favor of production?

Mr. Harvey. Yes, sir; that is the intent of the bill. Of course, it might be found by experience that that margin should be narrowed, or it might be found that it was necessary to increase that margin. In other words, it could be narrowed if the stimulation of or increased production was more rapid than the demand for goods. In that case you would want to slow down the investment in productive capital, because you would not want to have your production going too far ahead of your consumption, and producing the result that we had in 1929 and 1930.

Mr. Williams. As you proceeded from time to time with new inventions and discoveries of science, and with the increased facilities for production, with higher efficiency, greater skill, and better organization, of course the productive capacity would very materially increase, would it not?

Mr. Harvey. Yes. I think that there is no doubt about that. We hope so.

Mr. Williams. Do you think that the time would soon come under those conditions when the productive capacity would far exceed the ability of the people to consume?

Mr. Harvey. I think that the control of that, or the management of that, comes in largely under the methods of financing new developments, and that is a thing that this bill has not touched upon. It is a very interesting subject, and I hope to make a personal study of it before very long; but this bill is based entirely upon the question of production and consumption for use, and because that is, as the Brookings Institution has pointed out, the base of our capitalistic pyramid, and until we get that base more or less set, we cannot develop the safety point for the pyramid of capital investment and productive capacity. That comes outside of the mechanism of the bill altogether.

Mr. Williams. With this new development, or this increased development and increased capacity, that would necessarily mean a reduction in the cost of the product, would it not?

Mr. Harvey. Yes, sir; we hope. That is the rule of mass production, of course; that is one of the things that has made mass production a success.

Mr. Williams. And if the industries of the country were producing at 100-percent capacity, necessarily the cost per unit would be lower than if they were running at 50-percent capacity?

Mr. Harvey. Yes, sir.

Mr. Williams. What effect will that have on the retail cost?

Mr. Harvey. It might tend, of course, to reduce the necessity for the discount. The discount would be dependent more upon the tendency to save than upon anything else. It is the offsetting of this tendency to save that the discount is used for.

Mr. Williams. And is it the hope that within a few years, under this bill, you will get to the point where the discount will not be necessary?

Mr. HARVEY. Except at times. Of course, you always have swings. I think that there is no hope of getting perfect stability in this world, economically or in any other way. You have swings, and that discount is used as a sort of balance wheel.

Mr. WILLIAMS. Why have the 15 percent at all? Why not balance it?

Mr. HARVEY. I think, in order not to have an inflationary condition, it is better to have a margin of safety.

Mr. GOLDSBOROUGH. May I state to Mr. Williams that the reason that that was done, the reason that that margin was put in there—and it may have been unwise to do it, but every effort that could be made, that I was able to think of, was made in order to prevent the bringing about of an inflationary condition.

Mr. WILLIAMS. The thing that is still in my mind is this: That if the time comes when you will want to do away with the discount, and you have everything sufficiently balanced under the terms of this bill, and everything is moving along on an even footing, how much of this interbank currency do you think will have been issued and be outstanding?

Mr. HARVEY. That depends entirely upon the size of the national income. I think that with $100,000,000,000 of national income, it takes between thirty-five and forty billion dollars of circulating money to maintain it. Now, issued as the money is today, it sometimes is thirty-five or forty billion dollars, and sometimes only 20 billion. Issued with this balance wheel, it would be maintained around thirty-five to forty billion dollars. If the banks' credits were drawn in too much, we would tend to expand.

Mr. WILLIAMS. You are talking about the interbank currency?

Mr. HARVEY. Yes, sir. I am talking about the credit issue which is provided in this bill, whether you call it interbank currency or something else. It is an issue of credit to consumers, to balance the issue of credit to producers.

Mr. WILLIAMS. But I am asking you whether or not——

Mr. GOLDSBOROUGH. Mr. Williams wants to know how much of this interbank currency would be necessary, if it would be 35 or 40 billions of dollars.

Mr. HARVEY. I would say that that would be a fluctuating item.

Mr. WILLIAMS. What is your judgment about it?

Mr. HARVEY. My judgment, if I were going to manage that thing, is that I think I could manage it with about 10 billion dollars, and that most of the time, if it was managed properly, I would not have outstanding more than 7 or 8 billion dollars. That is my concept of the management of that fund, but it is difficult for me to tell this committee just how it would be done.

Mr. WILLIAMS. All right; that is your judgment, that it will take 10 billion dollars.

Mr. HARVEY. Yes, sir.

Mr. WILLIAMS. Is it your idea, and the fundamental idea back of this bill, that there is a very close relationship between the volume of money and the amount of business done in the country?

Mr. HARVEY. I think that that is the key to the situation.

Mr. WILLIAMS. You think that there is a very definite relation between the amount of actual money and the volume of business?

Mr. HARVEY. You are referring to bank deposits as well?

Mr. Williams. Yes.

Mr. Harvey. No. I think that that must be established. I think that that is what you do not have today, and what we are trying to establish.

Mr. Williams. I am referring to currency.

Mr. Harvey. Bank currency?

Mr. Williams. The amount of money in circulation.

Mr. Harvey. Currency is scarcely a factor.

Mr. Williams. There is really no real relationship between the volume of business and the amount of money?

Mr. Harvey. Between the volume of business and the volume of currency?

Mr. Williams. Yes.

Mr. Harvey. I should say very little.

Mr. Williams. It is a matter of credit?

Mr. Harvey. It is a matter of credit. May I say in that regard, to illustrate that, to support that point, that our circulation for 10 years before the bank trouble ran around from 4 to 4½ billion of cash, but our national income during that time increased from something like 65 billion dollars to 85 billion dollars without any corresponding increase in the amount of the currency in circulation.

Mr. Williams. What is your conception, or what is your definition of national income?

Mr. Harvey. Well, I go a little further than some other economists, because I split the national income into two different forms. The first form is what is known as national productive income, which is the volume of goods of all sorts, durable and otherwise, and consumption goods, which are produced at the current price level. That would be the national productive income, as economists call it, but there is side by side with that a different income, and which I have called—I have not seen anyone else calling it that—the national spendable income, which is what people spend. The income that they receive may be 85 billion dollars. The income that they spend, as a rule, is not more than 75 billion dollars. The rest of it is saved.

That is my interpretation of the meaning of national income.

Mr. Williams. Now, on that basis, what do you think that the national income ought to be, in order to furnish the people with what we need?

Mr. Harvey. I think that that has been established by various agencies on the basis of a comfortable sufficiency and economic security, and it ought, I think, to be, on the present price level, in the neighborhood of $1,000 per person for 130,000,000 people. In other words, we would not be really affluent as a Nation without an income of from 120 to 130 billion dollars.

Mr. Williams. That would be almost double what we have?

Mr. Harvey. That would be almost double what we have. You would not expect to go there all of a sudden. It would take from 20 to 30 years, but that is the income that I think that this Nation could very well have without debauching itself with too many luxuries.

Mr. Williams. What is this discount credit that is provided for in this bill, the national discount credit—is that the name of it?

Mr. Goldsborough. The interbank currency?

Mr. Harvey. The interbank currency.

Mr. Williams. No; this account that is set up in the Treasury of the United States.

Mr. Williams. This bill really does not call for an account to be set up in the Treasury. The previous bill called for an account to be set up in the Treasury known as the national credit account, which was the credit that the banks were not using and could not use because there was not a demand for it.

Mr. Williams. Maybe I got hold of the wrong bill, but I thought I saw it in here.

Mr. Harvey. I do not think it is there.

Mr. Williams. The national credit discount?

Mr. Harvey. The national credit account.

Mr. Williams. What is that? What establishes that? What determines what that is?

Mr. Harvey. That is the difference—that is the money difference, monetary valuation between the amount of goods used and the productive capacity. In other words, it is a credit that the banks would use if they could, but they cannot, because there is not a demand. What we are trying to do is to step up the demand which will validate that bridge there, or the difference between the two.

Mr. Williams. You do set up that account in the Treasury?

Mr. Harvey. We set it up as an estimate; yes, sir.

Mr. Goldsborough. It is not in the Treasury, but in the Federal Credit Commission.

Mr. Harvey. This bill does not call for a set-up anywhere. They simply use the index numbers for the discount, without setting up any arbitrary margin of credit.

Mr. Williams. What is this $10,000,000,000——

Mr. Goldsborough. It cannot be more than $10,000,000,000.

Mr. Williams (continuing). Which is provided for in this bill?

Mr. Harvey. That is to validate that credit that I spoke of, but it is limited. As a matter of sound legislation, it is proper and, I understand, good policy to limit and to state your values that you want to dispense.

Mr. Ford. Is it not a monetizing of the surplus products put into circulation?

Mr. Harvey. Yes, sir.

Mr. Williams. When you reach the situation when you no longer need the discount, and you have $10,0000,000,000 of this interbank currency in the banks of the country, then the question has been in my mind, and is yet, What is going to be done with it? You no longer need it.

Mr. Harvey. You no longer need it, because you have a sufficient volume of circulation. You have sufficient volume of bank credit. Then you call it in. You call it in by the same process that the Federal Reserve bank would call in money if it sold Government bonds. In other words, they would reduce the surplus reserves of the bank.

Mr. Williams. Call that in?

Mr. Harvey. Call that in in that way, by reducing the surplus reserves of the United States.

Mr. Williams. Then what would we put in its place?

Mr. **Harvey**. They would allow things to rest until it was necessary to put it back into the consumption pyramid.

Mr. **Williams**. Do you mean that the Government would recall that from the banks of the country?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. I still ask, What would be put in place of it?

Mr. **Harvey**. The only reason for recalling it would be if there was too much money in circulation. There would be no other purpose in recalling that money, except an excess of money.

Mr. **Williams**. The question that I have presented to you is this: You have $10,000,000,000 of this interbank currency out, and you have no longer any need for it, because you have a balance of production and consumption.

Mr. **Harvey**. Yes, but wait a minute. Isn't that 10 billion maintaining the balance? If it is, you do not want to recall it.

Mr. **Williams**. It is maintaining a balance on the bank books.

Mr. **Harvey**. I am talking about the balance of consumption and production.

Mr. **Williams**. But it has taken $10,000,000,000 to balance the books of the banks of this country, and it represents a credit which the banks gave, and which has been drawn out.

Mr. **Harvey**. But which remains as deposits in the banks.

Mr. **Williams**. It is in the banks, but now you say that they will recall it.

Mr. **Harvey**. Yes; if you recall the notes.

Mr. **Goldsborough**. You would not recall it if it is in balance. You would recall it if you get too much circulation.

Mr. Williams thinks that when you got enough, you would automatically recall this currency. You would not recall it unless your price level went too high.

Mr. **Harvey**. That is true, but we are talking about different balances.

Mr. **Williams**. After you stopped your discount, and you had things in balance, you would have that large surplus of money.

Mr. **Harvey**. That would depend upon what the view of the public was at that time for borrowing money from the banks.

Mr. **Williams**. Assume a condition where they did want to withdraw—and that is in this bill.

Mr. **Harvey**. That is assumed there in the bill. That is the reason it is in.

Mr. **Williams**. And that is a very wise provision, I think. Otherwise undoubtedly we would have inflation.

Mr. **Harvey**. Yes, exactly.

Mr. **Williams**. You would have credit possibilities that went beyond reason. If you put $10,000,000,000 more into the banks, and then had everything balanced, it would only be a short time, with your money reserves in the banks, until you had inflation possibilities beyond limit.

Mr. **Harvey**. Yes.

Mr. **Williams**. And it would become necessary to recall part of that money?

Mr. **Harvey**. Yes.

Mr. **Williams**. What would you put in place of it, to keep the books of the banks still balanced?

Mr. **Harvey**. You would not put anything in place of it. The banks would reduce their other credit balances, and the books of the banks would still remain in balance.

Mr. **Williams**. Let us get right down to it. How would they reduce their other credit balances?

Mr. **Harvey**. By calling loans.

Mr. **Williams**. There is already a liability against every deposit that they have.

Mr. **Harvey**. What is a liability?

Mr. **Williams**. I mean that there is already an asset and a liability balanced against each other.

Mr. **Harvey**. Yes.

Mr. **Williams**. And you call in one of the assets?

Mr. **Harvey**. Yes.

Mr. **Williams**. That creates an additional liability, does it not?

Mr. **Harvey**. No; there is no increased liability. Simply the deposits are reduced.

Mr. **Williams**. Yes; but they cancel each other.

Mr. **Harvey**. Yes.

Mr. **Williams**. You bring in an asset, and it cancels the liability that exists against that asset.

Mr. **Harvey**. Exactly.

Mr. **Williams**. That does not help your situation when you call in a million dollars of Government money, does it?

Mr. **Harvey**. Why doesn't it? The banks called in 15 billions between 1929 and 1933, and they did it by calling loans, and they reduced their liabilities that way.

Mr. **Williams**. But they used their assets with which to do it.

Mr. **Harvey**. They used their assets?

Mr. **Williams**. Surely.

Mr. **Harvey**. No, sir; they did not. They used the public assets, and they kept them in balance all the time. As they reduced their assets, their liabilities were reduced all the way down.

Mr. **Williams**. That is all right, but you have no asset to offset this liability that the bank owes to the Government, have you?

Mr. **Harvey**. They have got their other loans, an expanded credit situation.

Mr. **Williams**. I cannot understand to save my life how you are going to use other assets to offset this liability of the bank to the Government for this money deposited in the bank, without throwing the rest of it out of balance.

Mr. **Harvey**. I have here a statement of the bookkeeping of this, which I was going to put into the record.

Mr. **Williams**. I wish you would.

Mr. **Harvey**. I do not know whether I might read it to you, but I think perhaps you would see that the privilege of recalling this Government credit in the form of interbank currency or any other form is essentially the same thing as if the Federal Reserve bank recalls a lot of the credit that it has put out to the member banks, and it has gone out through the country. The customers have to realize on their assets in order to pay up their debts.

(The statement referred to by the witness is reproduced below:)

OUTLINE OF BOOK ENTRIES SHOWING HOW THE PROPOSED INTERBANK CURRENCY WOULD CIRCULATE

This currency, originating with the Treasury or Comptroller of the Currency, would be charged to the account of banks calling for it to validate discounts allowed.

Thereafter, taking a single bank for illustration, and assuming that it has received $2,000 of this currency and has credited its customers doing business as retailers $2,000 against discount vouchers, then the entries would be as follows:

Bank A

Customers' ledger		Interbank currency account		General ledger deposits account	
Debit	Credit	Debit	Credit	Debit	Credit
Current debits for customers' checks.	Current deposits plus $2,000 deposit for vouchers received.	Discount voucher deposits of customers.	$2,000 interbank currency from Treasury.	Total of customers' deposits plus interbank currency $2, 000.	Total deposits of customers' withdrawn.

Therefore—

Customers' general debits balance with general ledger deposit account credits.

Customers' credits arising from discount vouchers balance with interbank currency account debits.

General ledger deposit account debits arising from receipt of interbank currency balance with interbank currency account credits arising from its issue.

Result.—Interbank currency account in Bank A should always be in balance, and the same condition should continue as the currency circulates in other banks throughout the system.

Bank A would tender to its clearing house as settlement of an adverse balance a percentage of its holdings of interbank currency equivalent to the percentage that their total holdings of this currency bear to their total deposits.

The clearing house would maintain the same percentages in the settlements with banks having favorable balances. Banks receiving the currency from the clearing houses and not from the Comptroller for discounts allowed would write up their customers' credits just as if they had received Federal Reserve notes as part settlement.

It is not improbable that experience in handling these interbank currency notes might lead to their remaining in the Federal Reserve district banks, as credit reserves, and the circulation of the credits they give rise to might be recorded by the usual interbank book entries, in the same way the most of the transfers of interbank settlement balances are now made.

Under certain conditions some of this interbank currency would be automatically canceled and returned to the Comptroller. As for instance, when a bank loan is paid off in cash, or when a deposit account is closed out by the withdrawal of cash. And also when the general level of deposits is reduced.

One illustration of how this would come about is given below.

When a private loan is repaid to a bank whose deposits have been increased by the receipt of interbank currency a proportion of this currency would be automatically canceled, in the percentage they would bear to the total deposits of said bank.

In other words, suppose the deposits of a bank are $50,000,000, of which $500,000 has arisen from its holding of interbank currency; and suppose a customer of the bank draws a check for $1,000,000 to repay a loan, then deposits would be reduced by $1,000,000 and the total deposits now are $49,000,000, or a reduction of 2 percent.

Therefore 2 percent of $500,000 of interbank currency should automatically be returned to the Treasury.

Of course, no interbank currency would be returned if the loan was made for account of others, because the general level of bank deposits would not be reduced.

Mr. **Williams**. I think I understood you to say a time or two here that it was exactly the same as if the individual deposited, say, $1,000 in the bank.

Mr. **Harvey**. It is.

Mr. **Williams**. Don't you see a difference in that?

Mr. **Harvey**. I don't see a difference in that.

Mr. **Williams**. Between the proposition of an individual depositing $1,000 in the bank, and this proposition of the Government placing $1,000 in the bank to supply a deficiency that has already been made by reason of credit extended for something that they did not get? They do not get anything for that credit that they extended.

Mr. **Harvey**. Against what?

Mr. **Williams**. The 15 percent.

Mr. **Harvey**. Yes; the Government would get a credit.

Mr. **Williams**. What do they get?

Mr. **Harvey**. A prosperous country, to start with.

Mr. **Williams**. But what did the bank get? That is what I meant to ask, what did the bank get?

Mr. **Harvey**. The bank got nothing; the bank got a balanced account.

Mr. **Williams**. The bank got absolutely nothing. Now, if I go to the bank and deposit $1,000, there is a liability for that $1,000, but the bank gets the $1,000, does it not?

Mr. **Harvey**. Yes.

Mr. **Williams**. But in the other case the bank does not get anything to offset it; it gets no asset at all to offset the liability which is created by it to the Government when the Government deposits that money in the bank. The bank does not get anything, does it?

Mr. **Harvey**. May I ask this question?

Mr. **Goldsborough**. You started to explain it two or three times. Why don't you answer him?

Mr. **Harvey**. Because I want to answer him through this question. Mr. Williams says that the bank gets nothing when it gets this currency. I say that it gets something that is very intrinsically valuable.

Mr. **Williams**. I don't think that you understood me. I said that the bank got nothing when it extended this credit to the retailer for his 15 percent.

Mr. **Harvey**. It gets this commission for doing the business.

Mr. **Williams**. Here is a retailer that comes in, we will say, with $850 in cash, and he deposits that with the slips showing sales of $1,000, and he gets credit on the bank's books for $1,000. Now, there is $150 in there that represents this credit extended to the retailer, for which the bank does not get anything.

Mr. **Harvey**. Yes; it gets $150 from the Government.

Mr. **Williams**. It gets it from the Government?

Mr. **Harvey**. Yes.

Mr. **Williams**. It gets it from the Government all right. Now, when the Government withdraws it, who pays it?

Mr. **Harvey**. By the time the Government withdraws that money it will have gone into circulation in the general level of deposits, and the deposits will probably have very largely increased through additional loans that the banks will make. Those loans will be reduced when that currency is called in. The level of deposits will be reduced by calling in the currency.

Does that answer your question?

Mr. **Williams**. No; not to my mind at all, because you cannot reduce your deposits in the bank without reducing other assets of the bank with which to do it.

Mr. **Harvey**. The bank does not use other assets of the bank. It uses the assets of its customers.

Mr. **Transue**. Mr. Williams, may I ask a question there?

Mr. **Williams**. Yes.

Mr. **Transue**. This question comes down to this, as I take it from your statement: Either the Government has to pay that money to the bank, or the depositors of the bank have to pay it, or the bank itself, from its other assets, has to lose 15 percent in the final analysis.

Mr. **Harvey**. No, sir; the borrowers of the bank have to pay it.

Mr. **Transue**. The borrowers of the bank?

Mr. **Harvey**. The borrowers of the bank are the people who pay it.

Mr. **Transue**. How do they pay it back?

Mr. **Harvey**. Simply by having their loans called until the surplus reserves are sufficient to pay it.

Mr. **Transue**. Let us say that the bank lends $100, and if the bank calls that loan, the borrower has to pay back $100 plus interest?

Mr. **Harvey**. Yes.

Mr. **Transue**. And the $100 loaned to him is legally the depositors' money, is it not?

Mr. **Harvey**. No; the bank never loans the depositors' money. The depositors' money is on call for the depositor.

Mr. **Transue**. If a bank has 1 million dollars in its capital and surplus, and 10 million of deposits, and they lend that money out, whose money is it?

Mr. **Harvey**. Wait a minute——

Mr. **Transue** (interposing). Whose money is it that is loaned?

Mr. **Harvey**. It is the bank's credit which is loaned, because if the bank has 1 million of deposits on call from its depositors, it has 2 million dollars of deposits after it has completed that transaction, you see. It is part of the second million, or what they call the second deposit, that is called in.

Mr. **Transue**. I do not follow you. Will you say that again?

Mr. **Harvey**. If the bank has a million dollars in deposits, and it loans against those deposits another million dollars, then it has deposits in the banking system as a whole, as deposits, of 2 million dollars, doesn't it?

Now, it is not the first million dollars that will be called in, but the second million dollars that will be called in, what they call derivative deposits as the result of the loans, and it is those derivative deposits and those call loans that make the inflationary credit condition that we have been through.

Mr. **Transue**. I cannot follow you.

Mr. **Harvey**. Perhaps you do not understand how this deposit business, the loan and deposit business of the banks, works, but you will know the rule, I think, that every loan creates a deposit.

Mr. **Transue**. You mean that that money is taken out and put into commerce, and it goes back to the bank again?

Mr. Harvey. I mean that it circulates, but every loan creates a deposit. If you borrow $100 from a bank, you get $100.

Mr. Transue. Yes; but when they call those loans in, that money has to come from some place.

Mr. Harvey. It comes from the sale of securities or whatever has been borrowed on, or from the surplus account of the borrower, if he has one.

That is a routine banking matter, really.

Mr. Williams. Suppose that a retailer has been in operation for 2 years during the time that this discount has been in operation, and in that time he has received credits from the bank on account of the business that he has transacted, and discounts have been given to him to the extent of $10,000. Now, the bank has extended to him that credit, and the bank did not get anything from him for that, did it?

Mr. Harvey. No.

Mr. Williams. He draws all of that out of the bank, and quits business. Who pays the $10,000?

Mr. Harvey. You can say that he has got $10,000, and he draws it out in currency?

Mr. Williams. Yes. It is all placed in his account, is it not?

Mr. Harvey. How much would he draw out in currency, then? If he had received in that 2 years $10,000 of credits on the basis of 15 percent, he would have then to withdraw $15,000 in order to clean up the credit.

Mr. Williams. He has done that over a period of 2 years, or whatever it is.. Suppose that he has drawn out his account, including the credits?

Mr. Harvey. Then if it was drawn out in cash, and it was not returned to any bank, the bank could ask the Government to validate that demand for cash against the 15 percent, and the bank would have to meet the payment for cash to the extent of 85 percent itself.

Mr. Williams. He has put in 85 percent in cash, and he has a right to get that back.

Mr. Harvey. Yes.

Mr. Williams. And he has a right, in addition to that, to get the 15 percent for which he put nothing in the bank. Now, the question is, when he does that and quits the business, and leaves the country, who will pay?

Mr. Harvey. You say that he put nothing in. He puts his labor in. He put his business in, and he put his business risk in, and the public and the Government have got the benefit.

Mr. Williams. The bank did not get a cent, and it did not add a cent to its assets on account of that, did it?

Mr. Harvey. The bank got the Government guaranty.

Mr. Williams. Then you come back to the question, as I understand you. Now you say that the Government would simply have to pay it.

Mr. Harvey. It would in the case of a demand for cash of that kind. Of course, that is a very exceptional case, which is not general in any financial system.

Mr. Goldsborough. Mr. Harvey, there is no difference. If the public went to the bank and asked for cash, they could not get it, could they, under the present system?

Mr. Harvey. No.

Mr. Goldsborough. They could not get the cash, and there would be no difference whatever if this particular instrumentality was in the situation. Under the present system, if you asked for cash, as I said, you cannot get it, and that is what happened in 1933.

Mr. Williams. You do not mean to say that any business could not draw out any account over the course of years until that business closed, or the man running it went out of business?

Mr. Harvey. The situation would be precisely the same as it is today, except that the banks would be doing a better business.

Mr. Ford. You cannot deposit labor, time, and experience in the bank.

Mr. Harvey. Yes; but you monetize it every day and every hour and every minute, and that is what the Government would be doing under this bill, monetizing something that the banks cannot monetize.

Mr. Ford. I am a retailer, and over a period of 2 years I have gotten $30,000 out of my bank, and of that $30,000, about 15 percent of it has been in discounts received in the course of my business. All right; I suddenly decide that I want to leave California and come to Washington, and I go to my bank and I draw $30,000, and they pay me.

Now, in that there is $4,500 that they gave me as discounts, that I did not put anything in for. I still get my $30,000. The bank has got, in lieu of that $4,500 given me, interbank currency to that extent for that sum?

Mr. Harvey. Quite right.

Mr. Ford. And they find that they are going to need that $4,500 in their business.

Mr. Harvey. Who finds that they are going to need it?

Mr. Ford. Whatever people sent that back to the Government and asked that it be returned in currency.

Mr. Harvey. Pardon me; you say that the bank finds it is going to need it?

Mr. Ford. Yes.

Mr. Harvey. But the bank must manage its business so that it does not need it. It has no right to claim it. It only has a right to manage its business on its regular deposits outside of that. That is money that is to circulate only among the banks, and the banks cannot use it for any other purpose.

Mr. Ford. But suppose that there were several banks over the country on the same day that found themselves deficient in the sum of $4,500, and they needed that $4,500 for their business; they would have to take some valid assets and borrow the money, or else send the interbank currency back to the Government and get $4,500 in cash.

Mr. Harvey. I think that you are confusing the bank assets and those of the public. That 15 percent is the asset of the public, and not of the bank. The bank cannot use it.

Mr. Ford. There is a disappearing rabbit in the hat somewhere.

Mr. McGranery. Do I understand you to say, in effect, that the business of the bank would be divided into two classes, one of the out-and-out depositors of currency, and the other of the business done for businessmen?

Mr. Harvey. By means of checks?

Mr. McGranery. Of what?

Mr. Harvey. By means of checks, you mean?

Mr. McGranery. You used the term, "the public's assets," and "the public's deposits." What did you mean by that?

Mr. Harvey. I mean the deposits which we see reported today at 55 billion dollars.

Mr. McGranery. In other words, you would be doing two classes of business within the bank itself?

Mr. Harvey. Not at all. There would be only one class of business.

Mr. McGranery. Then why do you make that distinction between the one business and what you call its interbank currency business, or the public's business, as you put it?

Mr. Harvey. Because the interbank currency is designed so that it can only increase deposits dollar for dollar of the amount of currency issued, whereas a deposit such as you might make may increase the deposits by 100 percent or more.

Mr. McGranery. You are going to do both in this particular bank?

Mr. Harvey. This bank will do both, will run its own credit business, but it won't extend credit on the Government's money.

Does that answer it?

Mr. Reilly. Does this bill contemplate, or do you contemplate, through legislation, to compel banks to discount these credits?

Mr. Harvey. What is that?

Mr. Reilly. Would you, as a banker, give up good money in discounts for money that you could only use for certain purposes?

Mr. Harvey. How would the bank give up good money?

Mr. Reilly. When I as a merchant go to the bank and take in $100 worth of sales, and deposit $85, you give me $100 on a 15-percent basis, don't you?

Mr. Harvey. Yes.

Mr. Reilly. You put it in my bank account?

Mr. Harvey. Yes.

Mr. Reilly. And you as a banker have given out money that can be used, and you get for it interbank currency, and you cannot use that?

Mr. Harvey. No; because it has already gone out as credit.

Mr. Reilly. No; this is extra money.

Mr. Goldsborough said the other day something about the bankers having a great advantage by using this interbank currency. The bankers have purchased that; and they have given good money equal to the interbank currency. They have given money for it that can be used for all purposes, and they get money that they cannot use at all.

Mr. Harvey. They can use their own money, just as they have always used it, and they get an extra deposit that they can only use for 1-percent inflation, rather than——

Mr. Reilly. But is it not a fact that you would have banks under your system with two kinds of money, money that can be used for all purposes and money that can only be used for interbank currency purposes and bank balances?

Mr. Harvey. Yes; that is true.

Mr. Reilly. Now, if your bill were in force in 1929, 1930, and 1931, and the banks began to fail, there would undoubtedly have been billions of dollars in interbank currency in the banks?

Mr. Harvey. Yes.

Mr. Reilly. And the Government would have had to redeem every dollar of it?

Mr. Harvey. If the banks were put into bankruptcy, it would.

Mr. Reilly. If the banks failed, the Government would have to make up the difference?

Mr. Harvey. Yes.

Mr. Reilly. Isn't that another way of increasing the bonded debt of the country?

Mr. Harvey. There is no increase of bonded debt, but what it would do is to establish the greatest business that this country has ever had, and the money would be kept in circulation to the extent of those billions.

Mr. Reilly. That is true, but you have been trying to shy away from Government responsibility for these issues.

Mr. Harvey. The Government is responsible, but where we are differing is in this, that the Government has no responsibility to the banks. The Government is responsible for the money of the Nation, and the banks are merely trustees. That is the point.

Mr. Reilly. But the responsibility of the Government is that it guarantees the payment of every one of these interbank currency notes?

Mr. Harvey. If the public suddenly decides that it wants to do its business in cash, not only is the Government responsible for this money, but it would have to put it out, whether in that form or some other form.

Mr. Reilly. That is a speculation.

Mr. Harvey. No; that is a fact.

Mr. Reilly. The Government has not put it out.

Now, I have an idea that if you were Secretary of the Treasury, and you had been issuing this money and found out that the prices were skyrocketing, you would not recall it, but you would raise the bank reserves? You would require the banks to call for some more money from loans?

Mr. Harvey. You could do it either way.

Mr. Reilly. Are you not in favor of 100-percent bank reserves?

Mr. Harvey. Not at present. I think that 100-percent bank reserves would probably be forced. I have——

Mr. Reilly. Your bill goes toward that end, 100-percent bank reserves?

Mr. Harvey. Every bill and every bit of Government policy for the last 5 years has been going toward that goal, and there is no escape from that.

Mr. Reilly. I differ with you. One-hundred percent bank reserves, in my judgment, would put the banks out of business, and make them nothing more than cold-storage places for the placing of money.

Mr. Harvey. Of course, they would have a great deal of business, because with 100 percent reserves it does not mean that nobody would borrow any money. There would be a great deal of borrowing money, but it would be real money that they would lend, and it would be in the hands of syndicates. That is the way that they would do it. I do not know, human nature being as it is, that you are ever going to get away from lending money, but there is a big difference between lending fictitious money on 10-percent reserves and lending real money that has come into existence and is permanent.

Mr. **Reilly**. We built up our industrial system in this country on your so-called fictitious money.

Mr. **Harvey**. Yes; in that form.

Mr. **Reilly**. So you would do away with all of this lending by banks on credit?

Mr. **Harvey**. I said that I was not in favor of it. Please do not misunderstand. I think it is coming. I think, looking at the economic picture and the financial picture, if our democracy is going to live, and we are going on expanding our permanent money, eventually we will get to the point where 100-percent reserves is unavoidable.

Mr. **Reilly**. There are any number of students on banking who now differ with you on that question. We have increased our reserves recently because there was too much money in the country.

Mr. **Harvey**. Yes.

Mr. **Reilly**. Now you want to put in 15 percent more on all sales.

Mr. **Harvey**. Yes; but so much of the money is useless today; it is not doing its work.

Mr. **Reilly**. That is your opinion.

Mr. **Harvey**. It is in the banks, but it is letting people starve.

Mr. **Reilly**. That is your theory, but today the banks are loaded with money. I am getting letters every day from bankers on this bill to continue the prohibition against paying interest. They say that they have more money than they know what to do with, and that they cannot lend it.

Mr. **Harvey**. Why can't they lend it?

Mr. **Reilly**. Nobody seems to know how to fix that matter up so that we can get the purchasing power.

Mr. **Harvey**. That is what we are trying to do here.

Mr. **Reilly**. In 1929 the counter sales amounted to 50 billion dollars, and that does not take in electricity or the other things that are covered by this bill. But we will assume that figure of 50 billion dollars, and if this discount had been applied, it would have amounted to $7,500,000,000, and you would have in the banks of the country 7 billions 500 millions that could not be used to pay depositors, but that could only be used for your interbank currency work. Now, I do not know how you could limit it. The next year you might have to add 7 billion 500 million more, and where would it end—except, as you say, when prices got too high, you would throw them down. Do you recognize the quantitative theory of money?

Mr. **Harvey**. I do not know whether it it soundly established or not.

Mr. **Reilly**. I do not think that it has as much backing as it used to have, but it is that the value of an article depends upon the amount of money in circulation.

Mr. **Harvey**. What is that?

Mr. **Reilly**. The price of an article depends upon the amount of currency or money in the country in circulation.

Mr. **Harvey**. I would not agree to that. As the Brookings Institution has pointed out, it all depends upon where the money is.

The **Chairman**. He said in circulation.

Mr. **Reilly**. In the banks of the country, available for business.

We have about 6 billion dollars in circulation now, money in the banks, outside of the Treasury.

Mr. Harvey. Six or seven; 6 or 7 billion of currency in circulation.

Mr. Reilly. Outside of what is in the Treasury, there is about 6 or 7 billion dollars in the country?

Mr. Harvey. Yes.

Mr. Reilly. If you doubled that amount, which you would do under your system, prices would skyrocket, and you would have to give more than 15 percent discount after a while.

Mr. Harvey. Why?

Mr. Reilly. Because that is the basis of the quantitative theory of money. That great financier who came here 2 years ago and talked in favor of—I do not know whether it was the Goldsborough bill or not—claimed that if he had been President in 1933 and 1932, he would have shoved money into the world and kept the prices where they were, recognizing the quantitative theory of money.

Mr. Harvey. But he would have had an extraordinary experience if he had done it.

Mr. McKeough. May I interpose just a second? It is 12:12.

The **Chairman.** I am ready for the motion.

Mr. McKeough. I move that we adjourn.

The **Chairman.** Gentlemen, we will meet tomorrow in executive session to consider H. R. 7186.

(Thereupon at 12:13 p. m., an adjournment was taken until Friday morning, July 30, 1937, at 10:30 a. m.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

MONDAY, AUGUST 2, 1937

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other Members present: Messrs Goldsborough, Williams, Spence, Farley, Ford, Brown, Patman, Transue, and Crawford.

The CHAIRMAN. The committee will be in order. Our witness this morning is Mrs. Hawes.

STATEMENT OF MRS. HARRIET BOYD HAWES

Mr. GOLDSBOROUGH. Gentlemen of the committee, in looking at Who's Who, I find that Mrs. Hawes has had a very distinguished career. She was professor at Wellesley College until she was retired. She has made rather notable achievements in archeology throughout the Near East and I think is a thorough and consistent student of some of the acute problems that are confronting society.

I will ask Mrs. Hawes first to give the committee her background, if she will.

Mrs. HAWES. I am a Boston woman, educated at Smith College and the American School of Archeology in Athens; instructor at Smith College when I was younger and recently lecturer on art at Wellesley College, and retired this last year.

I explain that somewhat in the paper which I am about to present to the committee.

Mr. GOLDSBOROUGH. Very well, Mrs. Hawes. Will you please proceed in your own way?

Mrs. HAWES. Mr. Chairman and gentlemen of the committee, I appreciate very much this opportunity to speak for a half hour to the committee and shall be careful not to overrun that time. I shall not be technical but I hope to clear the air a little, which has become somewhat murky in these seven sessions.

May I begin by explaining my point of view? I speak, of course, as a woman, and since no other woman has asked to be heard, as representing, in a sense, half the citizenry of our country. I am sure you will agree that women suffer just as much as men from the effects of bad finances. But one thing I think you hardly understand; we women realize that men have produced the larger part of the material progress, but we also know that men are almost exclusively responsible for the mess today's world is in; for the fact that mothers' sons are killed and maimed on the battlefield, while mothers and babies at home are killed and maimed by flying men, against whom they have committed no crime and have no defense. I saw refugee women and children pursued by bombing planes in the World War and cannot forget it. The victims then were French; now they are Basque, Spanish, Chinese; but the bombing planes are a Yankee invention. Colonial women had less to fear from scalping redskins than modern women today must fear from men of the air whom all the world heroizes. So I may be wrong, but it seems to me men and governments have little cause for self-satisfaction in these times. We must also hold men chiefly responsible for the continuance of powerty amidst potential plenty, and this is my theme today.

I am an archeologist; at Wellesley College I taught the history of pre-Christian art. Art history has this advantage over political history: That it deals not with man's failures, his wars, and broken treaties, but his successes in producing things of beauty and for the continuous delight of mankind. Boondoggling seems to last better than almost anything else.

Two things have always interested me aside from my family—I have husband, children and grandchildren—these are archeology and public affairs. I am now attending the most interesting and curious university I have ever known—the sessions of our Congress.

You may think archeology a poor preparation for the study of public affairs, but it does provide a background; a vista. The archeologist is accustomed to think in terms of old stone age, middle stone age, new stone age—say 10,000 years ago—copper age, bronze age, iron age; the town I discovered and excavated in Crete—the oldest town, I believe, yet found in Europe—was of the bronze age, circa 1500 B. C., some time before Moses, 700 years before coins were invented, 1,000 years before Pericles. In one house we unearthed a kit of carpenter's tools, saw, ax, chisels; in other houses nails, awls, fishhoks, all of shapes exactly like our own, but all of bronze. Not a scrap of iron was found on the place. Now these homely finds are very convincing. They stretch the mind. Again, the acheologist is given facts from the earth which he must try to explain; he tries this and that hypothesis, finds it doesn't explain, rejects it, at last finds one that fits and sticks to it. So you see archeology is a training.

But you might still hold that with no experience in banking and currency, I can't judge at all of Mr. Goldsborough's bill. Perhaps not, but let us turn for one moment more to archeology. You are not experts in that line; yet I believe that in 3 hours, with a few books, charts, and two handfuls of potsherds I could prove to those of you who have minds trained in other matters, that the town I found dates from 1500 B. C., not 2,500 nor 500, and you would defend that judgment before critics, even if you couldn't restate in detail the ground on which it stands. This is my position with regard to this bill. Because it faces squarely the fact that we are no longer in the iron age, which lasted from about 1100 B. C. to about 1750 A. D., but are in the power age, and no longer in the phase of steam power but just over the threshold in the enormously more powerful phase of electricity, I am sure Mr. Goldsborough is on the right track. I know no other bill in the docket that faces this supremely important fact.

Of valid economics predating the power age there remains not a vestige. Of valid economics predating the intensive and extensive use of electricity there will soon exist only rags and tatters. We still have to thank Adam Smith for insisting "Consumption is the sole end and purpose of production"; but the old form of the law of demand and supply is outmoded, since supply has become practically inexhaustible. We have tapped the universe for electricity and for fertilizing nitrates; we shall be able to produce substitutes for any substance whose supply fails. We are already in the age of plenty, when not a single human being need want, but we do not admit it; we are using an utterly outgrown system of economics, and we are suffering frightfully from it.

This situation is so new and so decisive, I sometimes think all books written before the World War are antiquated, except the New Testament, or rather the Four Gospels, for St. Paul is in spots quite useless. But not the Gospels. The practical wisdom, for the new era, of those strange commands—take no thought for the morrow—consider the lilies of the field—is being revealed to our wondering eyes.

The puzzling parable of the laborer who had waited from early morning for a job and being hired at the eleventh hour, received the same pay as the one who had toiled all day, meets today's problem of unemployment. You remember the mysterious reference to a sin against the Holy Ghost, which was pronounced unforgivable? I am beginning to think our apathy in letting poverty continue in the midst of potential plenty is the unforgivable sin against the Holy Spirit, which is striving today for the good of all through science and invention. There need be no have-nots, whether there are jobs enough to go round or not. We are hearing today from the National Citizens' Committee at Johnstown of "The right to work"; Representative Ditter, of Pennsylvania, on July 5 said on the floor of the House, "Every American citizen has the right to work," but what they mean is a right to work when a job is given a man, and it is to the interest of the employer that he should continue at it! Other confusing phrases are in frequent use, for example, "Favorable balance of trade" when what is meant is a continuous tilt of trade in our favor. To an archeologist this looks plainly impossible; in the long run imports must equal exports or we go smash. Let us try to think straight. I believe Mr. Goldsborough is thinking straight, trying to solve a mathematical proposition, for which no man, no party is responsible, but which must be solved, if civilization is to continue.

I was pretty discouraged at the outlook, seeing the daily deterioration of a large part of our citizenry under want, uncertainty, and our necessarily cockeyed relief, and knowing that deterioration of citizenry is the greatest menace in the world to a democracy; so that section 8 of article I of the Constitution could surely be cited to justify any law passed for common defense against it. Then, in June 1936, the Democratic Party put this paragraph into its platform:

> We approve a currency which shall permit full utilization of our country's resources.

Why, that is all we need to put our people on their feet, make it possible for them to rule themselves, and resist any ism. If you gentlemen will take as your slogan "full utilization of our country's resources" and hunt for the way of making that possible, you will surely find it and you will be benefactors of the world for all time. For as the Commissioner of Education, Mr. Studebaker, has said in answer to his own question—

> Will democracy work in this new complex machine age? If we can make it work here to create an ordered social and economic progress resulting in the greatest good for the greatest number, it will spread by contagion * * * A democratic world is essential to a warless world * * * it counts noses and not corpses.

You may recall an experiment made some years ago with rats. So long as they were fed and had enough air, they lived peaceably together; then food was gradually withheld and air drawn out of the glass enclosure in which they lived. The result was they died fighting each other. Why shouldn't we have horrid strikes and hideous wars when the power of the universe is steadily rarifying human labor (if I may use the expression), and all enjoyment of life is withheld from those whose work is no longer needed. It is a tragedy of titanic dimensions.

Let us find out which of our Senators and Representatives realize this tragedy. In this respect, June 17 and 18 are historic dates.

On June 17 Senator Wagner said to Senator Bailey in discussing relief—

> I have listened to the claims of the Senator from North Carolina that there is no serious unemployment problem today. Does he not know that the very lowest current estimate of unemployment, that of the conservative National Industrial Conference Board, is 7,533,000, and that the average of all responsible estimates is about 9,000,000?
>
> What, in the Senator's judgment, has become of the 'technologically' unemployed? He must, indeed, be familiar with the tobacco industry. Nineteen hundred and thirty-six was a banner year for that industry. The annual return on invested capital surpassed that of 1929. Profits increased by 26 percent over those of 1935. At the present rate 153,000,000 cigars and cigarettes are being manufactured annually for every 100,000,000 that were made each year in the period 1923 to 1925. But, despite this huge increase of 53 percent in production, there are only 61 workers in the industry for every 100 employed in that earlier period. What has become of the other 39 percent? Has the employed tobacco worker of today benefited by this amazing technological advance? On the contrary, the average full-time employee is receiving a wage 20 percent below the 1923–25 level. Has the consumer benefited? On the contrary, he is paying the same old price for his smoke, or a little more. Who has gained? The employer, and the employer alone.
>
> Now let us look at it as a business question. To what does business owe its present prosperity, if not to the farsighted vision of the Government, in creating work and purchasing power and markets for goods through the use of the public credit?

I was attending classes at the great university of Congress that day and awaited eagerly Senator Bailey's reply. There was none; there could be none.

The next day Senator Bone made a truly remarkable speech, from which I quote a few passages. He began by saying:

> In presenting the figures I am going to employ, I want it clearly understood that I do not use them for the purpose of challenging the decency and sense of justice of any man in this country, although our economic machinery is so geared that it is now doing a very cruel thing to the people. The fact that it may not be studied or purposeful cruelty makes no difference, if economic misery and financial despair are visited upon a people, the practical effect is the same whether it be done deliberately or merely through the operation of a coldly impersonal economic machine.

He then showed a chart prepared by the National Industrial Conference Board and said:

> Mr. President, this chart is a study covering a period from 1914 to 1937, including the first 3 months of 1937. It shows that in 1914 the Board adopted an index figure of 100 for the factor of production, per man-hour, in our manufacturing industries. From 1919 to 1937 the production per man-hour in American manufacturing industries rose from approximately 100 units of production to 192 units of production per man-hour, representing an increase of approximately 92 percent.
>
> Now let us see what happened to the man-hours of labor in that period; that is the man-hours of labor required to increase production from an index figure of around 100 percent to an index figure of 192. The index figure of the man-hours of labor required to produce this tremendous step-up and increase in the tempo of production was around 120 in 1920, and from that point it dropped to around 90 in the year 1921, pursuing after that a rather devious course and winding up in 1937 with an index figure of 92; 100 less. There, in its heart and in its essence is the real reason for much of our trouble. We have a startling picture of fewer and fewer men turning out more and more products in the industrial life of America.

The Senator continued:

> The figures I am using seem to be a challenge to those who believe in preserving our present economic order. If we choose to ignore the implications of this picture and men are able to convince Congress that it is a mistake to adopt such a program as I have suggested (of shortening hours and maintaining wages) then we merely postpone the day of reckoning. I want to continue generous relief efforts, but I want the Congress also to drive straight at this problem of technological change. I think true statesmanship calls for this prompt and direct approach. History is replete with instances of stubborn opposition to change, and the apostles of laissez faire have closed their eyes to the fact that change is the law of life, that society is not a static thing and the ultraconservatives of our time, in so many instances, close their eyes to the fact that science is making over industrial society and thrusting upon us the terrifying problem growing out of an incredible productivity, going hand in hand with want and uncertainty, which is the everyday problem of millions of Americans * * * the continuance of this condition will destroy our economic machine.

Senator Bone was speaking chiefly of mechanized industry, but the report of the National Industries Board quoted in the Washington Post of July 21 says:

> The advance of technology in agriculture has tended to widen the gap in general well-being between farmers who are able to embrace it and those who are unable to utilize the fruits of science and invention. This gap is certain to widen * * * the man with the hoe and the man with the tractor are not competitive equals where they are engaged in the same type of farming.

Concentration of production upon fewer farms would compel smaller farmers to migrate to the cities to compete for jobs with industrial workers, the report said.

Senator Bone admitted there had been a rapid step-up in wages per man-hour in American industry as a whole, but presented figures from the Alexander Hamilton Institute which show that the total cost of labor—that is, the total amount of wages on which the Nation's purchasing power largely depends—was relatively low at the beginning of 1937; and this in striking contrast to the general impression created by the general increase in wage rates. For the total cost of labor depends not only on wage rates but on productivity per man-hour, and the latter was 71 percent higher in 1937 than in 1920. This explains why the total cost of labor was 12 percent lower than in 1929 and 41 percent lower than in 1920.

Senator Bone then cited the Brookings Institution as reporting—

> Despite the increase in population the number of wage earners in 1929 was lower than in 1919, whereas the production was almost 50 percent higher.

and remarked:

> I suggest to the Members of the Senate that we may no more disregard the ruthless implications of these figures than we can snub a cyclone or refuse an introduction to a buzz saw, going a million revolutions a minute, if we fall into it.
>
> Imagine a production of 50 percent higher in 1929 than in 1919 and yet requiring fewer men to attain that degree of production. We are now finding the cause of the thing we grapple with here today, and that is why I bring it to the attention of the Senate. We are dealing with effects and not causes when we pay out money to take care of the victims of this sort of a situation and, so long as we disregard or appear to disregard the cause and do not drive right into it, we are going to pay a sad price some time in the not too distant future.

Turning to the House:

Mr. Burdick, of North Dakota, Mr. Smith, of Washington, Mr. Mills, of Louisiana, Mr. Voorhis, of California, Mr. Allen and Mr. Dorsey, of Pennsylvania, sense the tragedy in full and have described it eloquently, but I need not quote the words of Representatives to Representatives.

Now as to remedies: Senator Bone adopts the plan of Senator Black to "shorten hours of work arbitrarily and maintain wage levels." He is not enthusiastic over this plan but says he knows no other to meet the situation. I certainly believe labor standards are necessary and the struggle for social justice will have to go on under whatever financial system we employ, but I also believe that unless there is a monetary adjustment such as that proposed by Mr. Goldsborough, the Black-Connery bill and all similar bills will result in continued scarcity and higher cost of living, which would go far to wipe out gains.

The Representatives I have named, with the exception of Mr. Dorsey, seem to understand symptoms better than causes of our economic illness and suggest cures which would not greatly help; as to the Townsend plan, mentioned by Mr. Luce and advocated by Mr. Smith, while I would welcome any addition to mass purchasing power, I cannot see how there would be any such addition, when the pension is raised by taxation; and as an old woman, retired for age, I shrink from the responsibility of spending $200 a month for the good of the country and from the certainty of being beset by a multitude of high-powered salesmen, who would wish to help me spend it. Let me say in passing that I wholly approve age limits and new blood for all faculties and all courts, even the highest.

To resume, Mr. Mills knows well the absurdity of a condition where there is a glut of things to eat, to wear, with which to build, while one-third of the people are hungry or ill nourished, poorly clad, and without decent shelter and warns that—

> as long as mass purchasing power stays down and continues to shrink (as Senator Bone's figures have shown it is shrinking) there will be an overproduction of bathtubs, cars, radios, and so forth, which we like to think are elements of the American standard of living.

Mr. Dorsey seems not far from Mr. Goldsborough when he says, July 8:

> The key to recovery and prosperity does not center in restricting production through deflation, but in increased consumption brought about by a better and

> wider distribution of the national income through an expansion of the circulating medium.

expansion, not inflation; there is a vast difference.

My own heart responds to a Jamboree of Boy Scouts, to bills backing the C. C. C., N. Y. A., vocational training, apprenticeship, but my mind recoils from the certainty that many of these young men on going out into the world will find their happy days over, their best aims thwarted, so long as jobs, markets, incomes are denied them by our outgrown system of economics.

May I now state my own conclusions? They are my own, not those of any cult, though they are in line with the thought of many other men and women, and are based on several books, just as your conclusion as to the age of my town would be based on my arguments, if you did me the honor to accept them.

In 1928 a young Englishman, Maurice Colebourne, wounded in the World War, published in America a book called "Unemployment or War" in which he faced the dilemma which presents itself to several nations today. The book was quickly sold out; he has brought out three enlarged editions under different titles. Like Mr. Goldsborough, I find the writings of Douglas on the New Economics obscure, although I am greatly indebted to him. He writes as an engineer and British terminology is somewhat different from our own; but I can understand Colebourne. He is sometimes restfully flippant, but he follows through convincingly, in my opinion, to this short summary of required action:

> Measure yearly the value of the nation, and declare yearly according to this value both a national discount through the price factor and a national dividend. Do these things through the exercise of a nation's sovereign right to control its own monetary system, having reinvested the nation with that right through legislation.

Mr. Goldsborough's bill sufficiently explains the measure of the Nation's value, which is based ultimately on our natural resources, plus the cultural heritage, intelligence and industry of our people, and can be determined as accurately as the expectancy of life, on which insurance is based. I am very sure, a couple of centuries ago, people would have said that it is perfectly ridiculous to think of having any life insurance; how can you ever tell how long A or B or C is going to live? Mr. Goldsborough's bill explains also the national discount through the price factor, which is C/P, the ratio of total consumption to total production in the preceding given period, and is Nation-wide in application. Mr. Goldsborough's bill makes no mention of a national dividend, and I am willing it should wait till Federal Government debts are substantially reduced, taxes brought low and the United States can afford it. There is no reason why a part of the appreciation of our country's real wealth, which we cannot check and God forbid our wanting to check it, should not go into a dividend for all, with no more shame attached to it, than is attached to the dividend a few of us are lucky enough to enjoy today. I could easily explain the connection between cultural heritage and national dividend if it were desired. The national dividend would take the place of our relief, our pensions, and so forth; it would put an end to as much bookkeeping as the national discount inaugurated, and it would preserve the self-respect of our people which is being sapped today. Do not forget, Mr. Goldsborough's bill

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In answer to Mr. Patman's fears about administrative detail, I would quote from Mr. Colebourne's book.

As to the national and retail discount:

> It is a question merely of deciding on the best technique, for making the national discount effective to consumers. * * * It is no criticism of the proposal to suggest that the difficulties of administering it would prove insuperable, when we have at our disposal a banking system, an industrial system, and a Government organization, which among them already perform, in their present-day routine, wonders infinitely more complicated than those which would be required to make the national discount effective. Again, only a wilful obstructionist would maintain that it would be impossible to apply the national discount to the purchase of a pennyworth of sweets by a child in a village shop, with such an example as that afforded by the cooperative societies under his nose. These, which number their consumers at about one-fifth of the entire population, appear to find no insuperable difficulty in not only keeping a record of every single purchase from a half penny upwards, but also in recording every purchase in the personal account of the consumer concerned, and, in addition, keeping current, deposits, savings, investment, and club accounts for many of their consumers, and, finally, paying a periodical dividend in cash based on the total amounts of purchases made by the total numbers of consumers, in the society concerned. What work there is, the cooperative discount and the cooperative dividend make it worth while to do; consequently it is done gladly, efficiently, and without fuss. In short, the important thing is to know what we want; the technique for doing it will follow and will be of the best. For however disastrous some of our policies have been in the past our administration of them has always been superb. (Cf. International Post Office Service.)

And I should like to think that we can do as well as the British can do.

As to the national dividend, Colebourne says:

> The technique for distributing the national dividend, as in the case of the national discount, is a matter of administrative detail. A nation which successfully kept accounts for about 7,000,000 of its citizens during the distractions and disturbances of war, and which kept other accounts for the dependants of these and distributed money by them by means of quarterly books of drafts cashed weekly at the local post office has no occasion to balk at the idea of distributing a uniform dividend to its citizens in time of peace.

Answering the member of the committee who believes the international bankers are responsible for the deadly mess we are in—a mess that gives women today as they read the news or listen to the radio, the unhappy impression that they are spectators as a lynching of the two youngest democracies in the world, I quote Douglas in one of his less obscure moments. He says, in his Monopoly of Credit:

> It is doubtless a misconception to accuse financiers of deliberately planning wars, suicide waves, bankruptcies, and the many other tragedies associated with the existing state of affairs. They are in the position of the immoderate drinker whom it would be absurd to suppose desires delirium tremens. He will do everything possible to avoid delirium tremens—except stop drinking.

For uncontrollable thirst the financiers substitute the appetite of greed, and I believe that the new economics would greatly restrain that appetite.

Now, as to the question how long it must be before such ideas as those of Mr. Goldsborough and Mr. Colebourne are accepted, I can only say an archeologist should be patient, taking a long view of things, for we are well accustomed to derision with a happy ending. Men as wise as any on this committee called Dr. Schliemann a "crackpot," yet he went on and found Troy. Dr. Evans, now Sir Arthur Evans, was laughed at for his surmise that there had been a pre-Phoenician script from which our alphabet is derived; later he found more than 1,600 tablets inscribed with this script.

In the last year I have been much heartened by a moving picture, The Life of Pasteur. Decades passed before the ideas of Louis Pasteur were accepted by experts. He was called charlatan, just as the new economists are called charlatan by those very experts in universities and schools and business administration who were absolutely ineffective in meeting the depression. Mr. Patman's questions about the effect of Mr. Goldsborough's bill on direct sale of eggs by farmers to housekeepers, on second-hand trade in motor cars and on licenses, other questions as to fraud and chiselers made me imagine the way Pasteur would have answered analogous questions. Suppose when he was seeking to demonstrate the true nature of infection, and a way of avoiding it, a hearer had asked him how to operate for brain tumor or gallstones. He would probably have answered: "I cannot tell you, I am not a surgeon, but this I can say with certainty; if you do not accept my theory and act in accordance with it, you can never be sure of performing any operation safely, no matter how simple it is, or how skillful you are in other respects." Briefly, the Pasteur theory is not a panacea but a sine qua non and the same I believe to be true of the theory presented in this bill—it is not a panacea but a sine qua non. If you can find a better technique, good. Mr. Goldsborough invited your cooperation and that of Treasury officials and bankers.

But we continue the old methods at our peril. And I think the daily news confirms that 1,000 times over.

I thank you for listening; and if there are any questions that I can answer, I will be very happy to do so.

Mr. Goldsborough. Mrs. Hawes, I am sure that I voice the sentiment of the committee in saying that we are deeply grateful to you for appearing, and that your statement has been of distinct service to the committee in its attempt to reach a solution of the tremendously difficult problem which you have been discussing. And in the name of the committee, I thank you very much, indeed, for appearing.

Mr. Crawford. May I ask Mrs. Hawes a question?

Mr. Goldsborough. Of course.

Mr. Crawford. I ask this question so that we will clearly understand what she said.

Did I understand you to commend the Federal Government for the actions it is now taking in connection with extending credit, and the use of national credit, in the form in which it is now being used? Is that what you meant to say?

Mrs. Hawes. Why, yes. But without this more scientific approach, I think it is going to result most certainly in an increase of debt. I wrote the President to that effect a year and a half ago. I am thoroughly for the New Deal, but I just think without the proper monetary adjustment the debt will grow larger and larger, and unemployment, technological unemployment, which is the thing, will grow greater and greater necessarily. It has nothing to do with who is President or anything else.

I think we are temporarily easing things by the issuance of this national credit. I think that Senator Wagner was right. I was quoting from him, you know, where he said, "Didn't they understand the business side of it—that really the improvement was due to this issuance of credit?"

Well, now, the point is, they are issuing the credit but not on any scientific system. They are issuing it as a form of debt.

I thought it had been demonstrated—and I have heard it spoken of, too, on the floor of the House several times—that people are beginning to realize that to pay the banks for issuing their own credit is really ridiculous.

Mr. **Crawford**. Then I must have misunderstood you, because——

Mrs. **Hawes** (interposing). I was quoting from Senator Wagner. Shall I read it again?

Mr. **Crawford**. I was coming to the conclusion that you were giving your personal approval to the present policy of increasing the national debt.

Mrs. **Hawes**. Oh, no; not at all. I was not giving my approval, except it is sort of fending off disaster.

Mr. **Crawford**. Acting as a buffer until something else is done?

Mrs. **Hawes**. Yes; acting as a buffer.

Mr. **Crawford**. That is what I wanted to bring out.

Mrs. **Hawes**. Of course, the President and the Government cannot do anything until they have a backing.

Mr. **Ford**. Mrs. Hawes, I have listened with a great deal of pleasure to your very clear and very philosophic conception of this problem.

I am thinking of this phase of it. Is it not one of the fundamentals of modern industrial practice to produce more goods at less cost; and is not the crux of the situation right here, that while it is less costly to the individuals who control that production, they are very often loath to distribute the benefits of that low cost to the ultimate consumer because of withholding, from a wage standpoint, a sufficient amount to increase their purchasing power?

Mrs. **Hawes**. I think, Mr. Ford, that is only a part of it and not the fundamental thing. I think the fundamental thing is that for every bit of production, wanted production, anyway, there should be a ticket, so to speak. You must monetize the full credit based on the full national wealth, or else we will continue to have difficulties.

I think your suggestion that they do not distribute the gains from the diminished-cost operation is perfectly true. But I do not think distributing it would solve the difficulty.

Mr. **Ford**. Would not that be the equivalent of the discount that this measure calls for?

Mrs. **Hawes**. No; I do not think so, Mr. Ford.

Mr. **Ford**. Of course, that is a case of two minds not meeting. But it is a fundamental of a modern age to produce more goods at less cost.

We will take that as an isolated thing. That is industry's aim and goal.

Mrs. **Hawes**. Yes, but that is not the answer. I was very much impressed by that simile of Mr. Munson the other day. I had never heard it before in my life; that is, about the way people are brought into the world and they all die, and it looks as if therefore the population were stationary. But it is not so at all, because the rate at which they are being born is faster than the rate at which they are dying.

I think that it is not merely that they are not distributing all of it in the way of wages and salaries and dividends and reasonable profits. I believe that profits will, in time, be controlled, just as interest today is controlled. One hundred, one hundred and fifty, years ago there was no control on interest. Now there is a control in various ways, so that we do not have usury. So I do not think that we will always have excessive profits. But that will not do it all, because all the time there are these deferred payments, and with expanding industry they will never catch up. And the more machinery is used the more effectively power-driven machinery is used—and it is power-driven machinery that we are up against—the more that gap widens.

Mr. **Ford**. I was just wondering whether there was any legislative remedy for something that is deeply ingrained in the philosophy of industry. Where a man has a plant that produces goods his aim is to produce goods at the lowest price and sell them at the best price he can get.

Mrs. **Hawes**. There is no harm in that.

Mr. **Ford**. There is a gap there.

Mrs. **Hawes**. There is always a gap that has to be filled.

Mr. **Ford**. You say, then, that that gap ought to be filled by the monetizing of Government credit?

Mrs. **Hawes**. That is it.

Mr. **Ford**. Say the country produces a hundred billion dollars' worth of goods this year, and when they come on the market there is only purchasing power for $85,000,000,000 worth, but the Government steps in and gives them a 15-percent dividend through what we call interbank credits.

Mrs. **Hawes**. Yes.

Mr. **Ford**. There is $15,000,000,000 of credit based on the surplus products of industry?

Mrs. **Hawes**. Yes.

Mr. **Ford**. And the Government undertakes, through the medium of its issuing power, to take that much?

Mrs. **Hawes**. But that is only issued when the sale is made. That, I think, is really a very ingenious device. I think we are in accord that there must be more purchasing power for the people, but how can we issue that purchasing power with the least harm? How can we issue it without bringing about inflationary prices? I think this retail discount meets that. I also think a national dividend meets it by giving to all a share in the country's wealth, and not putting a premium upon whimpering.

I have had quite a good deal of contact with people in connection with relief, and that leads me to say that the person who whimpers the most is the one who gets the most return. That is what I mean by the deterioration of our citizenry.

Mr. **Ford**. I am just exploring the subject. Would we not be likely to put retail merchants as well in the whimpering class?

Mrs. **Hawes**. No. But I will leave this to the gentlemen here, because I think Mr. Goldsborough and the others can answer you in language which meets your mind better than my language.

But so far as this discount is concerned, I do not see that there is any whimpering any more than there is in a bank discount now.

Mr. **Ford**. But a bank discount is different. A man goes to a bank and borrows a thousand dollars, and they discount his note, say, at 4 percent. They take $40 and give him $960. That is what he pays for the use of that money, on the basis of the rate of interest for a year. He pays $10 for the use of it for 90 days, and he has to pay that back in the very same kind of money.

Mrs. **Hawes**. I see; you are getting to a point that I had hardly touched upon. I think you are coming to the point that many of us think about, of getting something for nothing.

I said I thought I could explain easily the basis of the cultural heritage, and we are coming to that.

Let us take the case of Edison. You would think of him at once as a man who fought his own way. I think he was a newsboy on trains, making his own way, and later making the wonderful discoveries that were of such tremendous importance and benefit to mankind. We think of him as a marked example of rugged individualism.

But what do you think he could have done if there had not been any library books to which he could have had access.

I spoke of the situation that existed on this continent at about the time the continent was discovered, in the sense of the inheritance that the inhabitants of the continent at that time had.

They had exactly the same natural resources in 1492 and earlier as we have today, or a little more, perhaps. And they had a somewhat intelligent and very active population in the way of Indians. What is the difference?

People came from Europe with a cultural heritage. You could not say that A had it and B did not have it, and so on. It is distributed among the whole community, with an appreciation of the real wealth of our country that goes on generation after generation. That is what I speak of, and we would not want to check it. That appreciation does belong to the community, and it is not something for nothing. It is not that one person inherits it and another person does not.

They need not be one bit more ashamed of cashing in on the retail discount than we are ashamed—that is, the few of us who are so fortunate—of cashing in on our dividends.

It is unusually a matter of chance if only one person benefits from the inheritance. If there are a number of people in the family, the inheritance is divided among them. But if, for any reason, there is only one child, that child is very rich. There is no more reasonableness, in my mind, in the present inheritance tax——

Mr. **Ford** (interposing). You are attempting to substitute a certainty for an uncertainty.

Mrs. **Hawes**. Yes.

Mr. **Ford**. You say we have as many natural resources as we had in 1492.

Mrs. **Hawes**. Perhaps we have less.

Mr. **Ford**. We have less physical resources.

Mrs. **Hawes**. Yes.

Mr. **Ford**. But science has come in and increased the lesser to the greater, by reason of a broader and more intelligent utilization.

Mrs. Hawes. Exactly.

Mr. Ford. I am still thinking—we had gotten to the point of a national discount. Let us cut out the whimperer. Let us say they would not whimper.

The retailer takes his dividend, or his discount to the bank. The bank gives him the currency for 15 percent of his gross business. The bank, in turn, calls on the Treasury for interbank currency to make up that deficiency. In a system of bookkeeping there has been a large order that is a bank credit. Let us leave that out for the moment.

Over the course of a year's business, assuming it amounted to $100,000,000,000, the banks have $15,000,000,000 of interbank currency in their vaults, good only to circulate among themselves.

Mrs. Hawes. Now, if I may interrupt, you are getting distinctly to the technical side. The previous bill introduced by Mr. Goldsborough did not use the term interbank currency. If I were writing a bill I might not use that term "interbank currency."

What I am trying to get at is this: If we are going to meet the difficulties of this power age and meet them successfully, we have to monetize all of our real wealth, and you gentlemen, members of this Committee on Banking and Currency and others like you will find the way. We cannot say it is impossible when we have the radio and the telephone going around the whole world. I am as sure as I am that I am sitting here that if you will put your minds to it and realize the difficulties of this power age and then go out to meet them, you can meet them, just as scientists have met the difficulties of the power age.

Mr. Ford. I can appreciate what you mean by the monetizing of national credit, but I am a little bit hazy——

Mrs. Hawes. Let me find a better way of expressing it, Mr. Ford.

Mr. Ford. I do not care what you call it; the fundamental thing you are talking about is the monetizing of the national credit.

Mrs. Hawes. Yes; the expanding of national credit to keep parallel with our ever-expending wealth.

Mr. Ford. I am thinking of this phase of it. If the Government could do that, then no government ought ever to owe a dollar.

Mrs. Hawes. Mr. Luce the other day clearly said he did not want to owe a dollar. We would not have these terrible wars if it were not for these things. You know what has happened. They cannot dispose of their goods in a particular country so they try to force them on the markets.

This may interest you. I keep clippings, and I came upon this one not long ago. It is very yellow, which shows that it was published before the World War. It is headed Stir Up War Talk to Make Business—German Contractors Aid French in Anti-German Scares—War Minister Admits Part of Charges.

That was before the World War. And that is what is going on now.

I can tell you, to a woman that is pretty discouraging. If we felt that really this thing could not be met and managed I would very much doubt whether we would think that life was worth going on for very long.

Mr. Ford. I happen to have made a study of foreign trade in 1920. Scribner published a book called the Foreign Trade of the

United States, which Mrs. Ford and I wrote. We spent a couple of years in Europe studying that subject, so I am more or less familiar with it, insofar as one can be familiar with what you call our outmoded economic system.

So I look at the question of foreign trade not from the standpoint of profit and loss but as a means of the increase of health, wealth, and happiness among nations by a sort of free exchange of their goods.

For a number of years the United States had what was known as a $500,000,000 balance of trade, but it was not.

Mrs. **Hawes**. It was not a balance of trade at all.

Mr. **Ford**. It was known as a favorable balance of $500,000,000.

Mrs. **Hawes**. You cannot have in a balance of trade a favorable balance.

Mr. **Ford**. We did not have a favorable balance of trade; we have had a favorable physical balance. We sent 66⅔ percent of our cotton to Europe and to the Orient. We sent 25 percent of our tobacco, and 73 percent of our corn, in the form of pork products, and as a result, when the books were balanced it was said there was a $500,000,000 favorable balance for the United States. But that was absorbed through the interest we owed to Europe on the six or seven billion dollars of loans on stocks that they owned in this country, and $75,000,000 that we paid to European insurance companies for the insuring of our goods which are sent across the ocean, and also practically $170,000,000 which foreigners here sent home in the form of remittances, and the balance was taken up by the tourist trade and the freight that we paid to carry our goods across the ocean. The freight and insurance amounted to about $160,000,000.

When you total those items, the actual balance was a little bit against us. Sometimes it was 12 or 15 million dollars in our favor, and sometimes 12 or 15 million dollars against us.

At that time a lot of our surplus corn and of our surplus cotton, and practically all of our surplus tobacco, and also a lot of our surplus farm machinery was sent abroad. Then the automobile began to supplement those things. Up to the time of the war that was the situation.

Then suddenly foreign governments, in order to get credit in this country—we took over their stocks and bonds, and pretty soon Europe finally owed us a tremendous sum. There are no exact figures on that.

Then we started with an adverse balance against Europe of about $20,000,000,000. We had sent Europe $20,000,000,000, and we sent her $20,000,000,000 worth of goods, and here we are insisting upon the collection of that $20,000,000,000 of goods, and we are unwilling to take it in the same kind in which we sent it.

That has been one of the unbalancing factors in our economic system, in our economics all the way through.

And until such time as we are able to absorb more and more each year and bring back the goods we sent over there, we will never get them back, they will never pay for them.

Mrs. **Hawes**. In connection with this cotton business, my son was in Egypt and he saw things that went on in Egypt at first hand.

Of course Egypt is producing enormous quantities of cotton, and India is also producing great quantities of cotton, they are supplying their own market and taking the market from our southern cotton because they can provide it to better advantage, and we have to accept that fact and have to develop more and more our own domestic market.

Mr. **Ford.** We undertook to meet that situation by buying foreign securities, did we not?

Mrs. **Hawes.** Yes. But you are getting beyond my depth now.

Mr. **Ford.** We bought a good many of their foreign securities that were not good?

Mrs. **Hawes.** I know most of those foreign loans have proven to be a very bad investment.

Mr. **Ford.** For those foreign securities we did not send them money; we sent them goods.

Mrs. **Hawes.** We sent them good stuff and we got in return worthless commitments.

Mr. **Ford.** All over Germany, for instance, you will find qualities of high-class American material; we never sent them a dollar in money.

Mrs. **Hawes.** I know that.

Mr. **Ford.** Coming back to the 15 percent, I wonder if a system of this kind of monetizing national credit were developed, whether we could take a step forward and monetize international credit. That is what I am getting at.

Mrs. **Hawes.** As I understand it, we talk a lot about foreign trade, but it is a very small percentage compared with our domestic trade.

For that credit certainly I think we would have to have money, international money based on gold. We have plenty of gold that could be used for just that purpose, for the financing of trade between nations.

But as to those things, Mr. Ford, I am very sure we should not, if you will excuse my speaking very frankly—we should not waste time in trying to think how to solve them. I am thoroughly of the opinion of the First Lady of the Land, who on Saturday last had this to say in her column in the Washington News, after she had had an interview with Mr. and Mrs. Elliott of England, who knew all about cooperatives.

(The statement referred to was not submitted.)

Mrs. **Hawes.** That is the point of view of Mrs. Roosevelt, and it is also my own idea.

I thank you very much for your patience in listening to me, Mr. Chairman.

The **Chairman.** We thank you very much for your statement. It has been very interesting and I am sure very helpful.

(Thereupon, the committee adjourned, subject to the call of the chairman.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

MONDAY, JANUARY 31, 1938

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:48 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Farley, Mr. Meeks, Mr. Koplemann, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeogh, Mr. Evans, Mr. Transue, Mr. Wolcott, Mr. Gifford, Mr. Luce, and Mr. Crawford.

The CHAIRMAN. The committee will come to order, please.

Gentlemen, we are here to resume hearings on H. R. 7188, introduced by Mr. Goldsborough; and Mr. Goldsborough will now discuss the bill further, if that is your desire, Mr. Goldsborough.

Mr. GOLDSBOROUGH. Yes, sir.

The CHAIRMAN. The committee will be glad to hear you.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. GOLDSBOROUGH. Mr. Chairman, the bill H. R. 7188 was discussed in the last session of Congress before this committee rather fully, but I am sure that the members of the committee are not just fresh on it, and I am going to take the liberty of going over it very briefly. In doing that I am going, in the first instance, to use some extracts from those who have attempted to analyze the provisions of the bill.

The bill was analyzed in the September 2, 1937, issue of the New English Weekly, a magazine published in London. There is some of the article which does not bear directly upon the issue. It speaks in a rather complimentary sense of me, but I will confine myself entirely to the part of the article which undertakes to analyze the discount.

The CHAIRMAN. I take the responsibility, without having seen the account, of incorporating that part in the record with regard to you. We would be glad to have that.

Mr. GOLDSBOROUGH. The author of the article says:

> After careful study of the speech with which Mr. Goldsborough introduced his previous bill, the speech with which he introduced his present bill, and his evidence to the Committee on Banking and Currency of the House of Representatives, I appreciate all the more one of his claims:

"I say with the utmost seriousness that I would like to discuss the validity of this proposed measure with any man in the world, and I am not at all afraid of the result. My friends on the Committee on Banking and Currency will, I believe, bear me out when I say that I am cautious in making statements of that kind; but I have struggled with this thing too long not to believe that I do not know something about it."

Both on the basis of the well-received, magnificent addresses of Mr. Goldsborough and my news from the American movement, I share the hope that this measure will, after examination by the committee, be introduced into Congress.

Tempted to quote at length from Mr. Goldsborough's brilliant addresses, I confine myself to a brief statement of the contents of the bill:

(1) *Administrative.*—The rate of discount will be determined by a Federal Credit Commission. It will be applied only to sales by retailers to consumers, not to goods supplied for resale. Every retailer operating the scheme will be required to obtain a license or certificate of authority and to conform to all regulations established by the Secretary of State for fulfilling the terms of the act. The banks are directed to accept from retailers the vouchers which furnish the evidence that the discount has been allowed. The banks will receive from the Federal Credit Commission (national credit account) currency notes to the amount of the vouchers. These notes will circulate only between banks. They will thus provide reserves and money for interbank transactions, e. g., the adjustment of checks written by retailers and paid by the wholesaler recipients into other banks. The commissioners, seven in number, will be appointed by the President, for a term of years, and will be salaried and pensionable. "No person"—I like this and therefore quote it verbatim—"shall be eligible for appointment as commissioner unless he is a citizen of the United States, and in the judgment of the President qualified to develop expert knowledge of economic, industrial, and statistical problems, and to perform efficiently the duties required by the act." The Commission will be able to employ such statisticians as it may require, and to call for statistical information from Government departments.

(2) *Basis of discount.*—For a start the discount will be a modest 15 percent, based on the certainty that the unused capacity of American industry exceeds that proportion. The Commission will determine periodically the value of unused capacity of industries and people of the United States for the production of wanted goods and services. This unused capacity will be the basis for calculating the percentage below cost at which goods will be sold to consumers in the forthcoming period.

(3) *Safeguards against inflation.*—No discount will be declared unless capacity to produce exceeds consumption by 15 percent. This, by the way, allows for lag if for any reason capacity is not increasing and demand is overtaking it. The rate of discount will not be raised by more than 5 percent at a time. If consumption should overtake production some of the credit issued by the Treasury at the instance of the Commission will be "called in" from the bankers, who will call in a portion of outstanding loans, not selectively, but in consultation with the Treasury. Banks may be required to raise their currency resources to 100 percent or more.

(4) *Sanctions.*—Until the discount figure for any period is declared, all information collected by the Commission is officially secret. Penalties are prescribed for falsification of sales accounts or costs, etc., and for any attempt to interfere with the Commission. Licenses are revocable in the event of breaches of the regulations.

It will be evident from the foregoing summary, which I have tried to make both brief and clear, why Mr. Goldsborough describes his "national credit control account" as a revolving fund for achieving a new kind of stabilization; the stability that proceeds from the equation of consumption with production, and the expansion of production to the totality of the Nation's requirements. Hence the title of the bill: "To provide a national monetary policy which will have a definite relationship to the requirements of domestic industry and trade under the conditions imposed by our power economy, which will increase production and consumption to the limit of the country's power to produce and for other purposes."

At the hearings during the last session, a representative of the American Retail Federation was in constant attendance, and in the bulletin of the American Retail Federation of July 8, 1937, the following analysis of the bill appears:

The Goldsborough Bill

PURPOSE OF THE BILL

The purpose of the bill, as stated in the declaration of policy, is twofold:

1. To adjust and control the price of commodities sold at retail so as to make it conform to the volume of purchasing power in the hands of the public.
2. To regulate the purchasing power so that production of wealth in this country shall be maintained in full measure.

The bill proposes to accomplish these ends by a discount in price on all goods and services purchased at retail. The idea has been likened to a national mark-down sale, except that the retailer is not called upon to finance it.

OPERATION OF THE RETAIL DISCOUNT

For the first 3 months the retail discount is to be 15 percent. Thereafter the rate of discount is to be set by the Federal Credit Commission, created by this bill, and is to be based upon the percentage which the idle productive capacity of the country bears to the total productive capacity.

For example, during the first 3 months merchandise at $10 would be sold to the consumer for $8.50. The retailer takes the cash he receives from the customer, together with a voucher, to show that he has given the discount, such as a sales slip, to the bank. At the bank he deposits the cash and the voucher, and receives credit for $10. The bank applies to the Treasury of the United States and receives $1.50 in interbank currency notes.

INTERBANK CURRENCY NOTES

Interbank currency notes are to be distributed to the banks to act as the basis for the retail discount. After they have been applied to that purpose they are to remain as a circulating medium within the banking system, and can be used in all clearinghouse and interbank transactions. These notes may be used by the bank as reserves, but not as a basis for expanding private credit in the form of loans built on fractional reserves; that is, banks may make loans based on interbank currency notes but only on a dollar-for-dollar basis.

Interbank currency notes are also made receivable for all forms of Federal taxation payable directly by the banks.

REGULATION OF MONEY

The regulation of the supply of money currency and credit is entrusted to two agencies:

1. The Federal Credit Commission (as created by this bill). The Commission, by means of the retail discount, puts new money into circulation. Whenever the Commission finds that an inflationary condition is tending to arise, it is to instruct the Secretary of the Treasury to call in interbank currency in a sufficient amount to establish and maintain monetary equilibrium. When notified by the Secretary, banks are to call in outstanding obligations in order to increase their reserve ratios. This will then permit the return of the interbank currency to the Treasury.
2. The Federal Reserve Board (as now constituted). The power of the Federal Reserve Board to conduct open market operations is continued. The power of the Board to raise and lower the amounts required for reserves is expanded, by allowing the Board to raise the reserve requirement up to 100 percent.

Aside from these two agencies, two provisions of the bill, already mentioned, restrict the amount of money in circulation. First is the provision which allows the interbank currency to be used only as a 100 percent reserve, and second the provision which allows the banks to use the new form of currency to pay all Federal taxes. These two provisions are intended to prevent an inflationary condition from arising.

Then there is a summary, reading as follows:

> Inflation has been described as the result of making purchasing power (currency and credit) available to the public at a faster rate than goods are made and brought to the market. The purpose of this bill is neither inflationary nor deflationary, since the added purchasing power (the retail discount) is made available to the public only after the goods have been brought to the market and sold. The purpose of the bill, then, is to expand the supply of money in the country so that the Nation may utilize to the fullest extent its means of production without causing a period of inflation, and without causing a surplus of unsold consumer goods.

I think I should state that the analysis made by the American Retail Federation is very satisfactory to me. The American Retail Federation is an organization which has its branches in every State in the Union, and serves a good deal more than half of the retailers in the United States.

Mr. PATMAN. The gentleman is familiar with the investigation of the American Retail Federation, is he not?

Mr. GOLDSBOROUGH. Well, I cannot say that I am. I think that there was an investigation made in the Senate.

Mr. PATMAN. No. I was chairman of the committee that investigated them in the House, and I do not think that the gentleman's statement is correct that they represent half of the retailers. In fact, they represent very few.

Mr. GOLDSBOROUGH. My conclusion is based on records that I have seen, and I do not think that I am mistaken about it. I know that there is a very good set-up in Maryland, and I am inclined to think there is throughout the country. It certainly is true, in my judgment, that the analysis made here by their economist is very fair, and, I think, very accurate.

Mr. Chairman and gentlemen, in order that I may have my point of view understood, I would like to make a contrast. In the state of nature, a man who starts out in life will go and get himself a piece of ground and build himself a shack, but after he lays in a supply of potatoes, turnips, flour, sugar, and tea, he begins to think about building himself a house, which he does. In building the house, of course, he uses up to a greater or lesser extent the supplies which he has been able to accumulate.

Now, when we deal on the installment system, as we are doing in this country to a much greater extent than anywhere else in the world, we are traveling absolutely contrary to what is general in the state of nature. For instance, in the housing bill, which will become a law in a few days, we say that the individual does not have to create for himself the means whereby he can get himself a house. We say that he shall have the right, provided that he can get the loan, to give a mortgage of 90 percent on the home that he buys, and the Federal Government—society—guarantees that that mortgage will be paid. So that, instead of accumulating funds to build a house, as he would do in the state of nature, he builds a house first, which means, of course, that under present conditions in this country—present monetary conditions in this country—he can never pay for his house, and when I say "he," I mean society collectively, and not one of them, because there are plenty of individuals who would be able to pay for the houses, but it is absolutely impossible under present conditions for the people as a whole who will take advantage of this act not to lose their property sooner or later if they buy it on the installment plan.

Now, I think that the main purpose, the main beneficial effect of this legislation, or of legislation like this, would be to enable the individual to accumulate for himself the resources necessary for the construction and the cheerful and happy operation of the permanent assets, such as a home, which makes for human happiness. In my judgment it can never be done under an economy based on debt. It never has been done on an economy based on debt. As long as your economy is composed of debt, it does not make any difference how much we produce; it does not make any difference how many labor-saving devices we create, and how tremendous becomes our power economy, as long as we base it on debt, for it can never be distributed to our people.

Mr. **Reilly**. May I ask a question?

Mr. **Goldsborough**. Just one second. I just want to quote John Stuart Mill. He lived a great many years ago, of course, and lived long before our so-called modern inventive age and power age. But the same rule applies now as applied then. He says: "Hitherto, it is questionable if all the mechanical inventions yet made have lightened the day's toil of any human being."

Mr. **Reilly**. Under your theory, a man should never build a house unless he has all of the money to build it?

Mr. **Goldsborough**. Oh, no; I did not say that. I did not intend to say that. I do not want to contradict you, but what I mean is that I did not intend to say that. I was only trying to contrast the natural order of things with the order of things based on installment selling, which I consider essentially unsound, and I say this, that as long as we attempt to create prosperity on an installment basis, where a man not only mortgages his present assets but his future earnings, you are bound to have these periodical crashes where prosperity is not resumed until a great portion of the debt is wiped out by bankruptcy and in various ways of compromise.

That is what I am talking about.

Mr. **Reilly**. All of our present-day prosperity is based on debt. Millions of farmers have bought land on debt, and paid it up. Are you going to stop that kind of procedure?

Mr. **Goldsborough**. Why, I hope, Mr. Reilly, that credit will be increasingly accessible.

Mr. **Reilly**. Perhaps you mean that credit is too liberal.

Mr. **Goldsborough**. Oh, no; I do not mean that. I do not mean that at all. What I mean is this, that the need for credit should be the occasional incident of national life, and not its necessary and eternal accompaniment. That is what I mean. You cannot do anything in this country now except that it is based on credit. All the capital, surplus, and undivided profits of all of the banks in the country, is less than 7 billion dollars. If we used only that money, everything in the country would stop right still.

So that the only way we can get circulating media in this country under our present set-up is through the practice of loaning money under fractional reserves, which means debt.

Mr. **Kopplemann**. Would you increase the media, Mr. Goldsborough, under your bill, so that I would find it unnecessary to borrow to buy goods in my business?

Mr. Goldsborough. Well, you might or you might not find it necessary to borrow.

Mr. Kopplemann. Would you make it possible?

Mr. Goldsborough. That depends altogether on the individual, but under this bill, very gradually the process of fractional reserves would be done away with, so that instead of having simply a reserve upon which you could lend from 5 to 10 times its amount, you would have in place of that real money.

Let me illustrate that as best I can—and the only way you can illustrate a new thing is by symbolism; you cannot state accurate figures, because you have not any precedent upon which to base them, but let us assume that this law goes into effect, and the Credit Commission decides in a little while that all the wanted goods and services which the country can produce are not being distributed, and they raise the discount from 15 percent to 20 percent.

I was told on Saturday by the Department of Commerce that the total retail sales in this country, including automobiles and transportation, but not including public utilities, such as telegraphs and telephones, are 40 billion dollars.

Now, let us assume that the retail sales to the ultimate consumer of telegraphs, telephones, lighting, and so on amount to 5 billion dollars. A retail discount of 20 percent, if it continued for a year, would require the operation of this retail discount to the extent of 9 billion dollars.

Mr. McKeough. Nine millions, or 9 billions?

Mr. Goldsborough. Nine billion dollars.

Well, now, in the first place it is entirely reasonable to suppose that after this discount operates for a short time, and consumption approaches production, so much more labor can be used, so much more employment can be given, that the discount rate will be constantly decreased rather than increased. But if you had to use the full 20 percent discount—which of course is incredible—for 8 years, you could, by increasing the reserve requirements of the banks gradually until you reached 100 percent reserve, operate this discount without the slightest bit of inflation, and guarantee full consumption to the extent of the country's power to produce, and you would have 8 years in which to devise amendments to the legislation, correct its defects, and have a program then which would perpetuate the consumption of the country's productive power, which of course is the purpose of this bill.

Mr. Ford. Will the gentleman yield?

Mr. Goldsborough. Just a moment, Mr. Ford.

I wanted to say one other thing, and that is that instead of hurting your banks, instead of hurting the established institutions which we call banks, you would be helping them. My God, they get gray-headed and they get bald-headed thinking about how to maintain the reserves, thinking about how to maintain this prevailing equilibrium that they have to do in order to try to avoid runs on their banks and bankruptcy. In addition to that, under this bill real purchasing power at the bottom is always guaranteed; you cannot have such a thing as a depression. It is impossible. You cannot have such a thing as bank failures, because as long as the masses of the people have purchasing power, everything else is bound to run, because it goes from the consumer to the retailer, then to the wholesaler, then to the manufacturer, and to the prime producer.

Mr. Kopplemann. I am very much impressed by what you say, Mr. Goldsborough, but will you in a like manner continue on the question of how you will find it possible to control inflation. Your presumed 9 billion dollars over a period of 8 years would amount to 72 billion dollars of new media of exchange.

Do you get my question?

Mr. Goldsborough. Yes, sir.

Mr. Kopplemann. How would you control inflation if you have that come into the picture?

Mr. Goldsborough. Of course, in 1929, Mr. Kopplemann, we had about 62 billion dollars in circulation based on this credit system under which we are now operating, and at that time, according to the investigation of the Brookings Institution, nearly half of our people were not on a proper subsistence basis, so that it is not unreasonable to suppose that at the end of 8 years, producing all that we can consume, and with practically all of our people on a proper subsistence basis, that the 72 billion dollars would not cause inflation.

Of course, when I fix the figure at $9,000,000,000, and assume the use of a 20-percent discount for 8 years, it is merely an assumption for illustrative purposes.

Mr. Ford. Mr. Goldsborough, I have been puzzled about one thing. Assuming that this 20-percent discount was operative over that period that you mentioned, and there was $72,000,000,000 worth of interbank currency in circulation between the banks, the Treasury would have issued that $72,000,000,000, would it not?

Mr. Goldsborough. Yes.

Mr. Ford. Of course, it is not interest-bearing; we understand that; just the issue of a note given in lieu of that 15-percent discount, but what provision have you made, or is there any provision or method whereby all of that $72,000,000,000 can ultimately be liquidated, so that the Treasury will not be responsible for it? Or, is this a Treasury obligation? Do you conceive it to be a Treasury obligation, or merely some kind of a symbol that the Treasury issues for the purpose of balancing the difference between production and consumption?

I cannot conceive of a mechanism of that kind going into our economy, because 15 or 20 percent is probably the margin between consumption and production, but if all of our mills, factories, and farms were producing at top speed, and we got to the point where this discount was no longer necessary, because it was going of its own momentum, the only danger I see in your proposition is that this $72,000,000,000—and we are assuming the maximum here—would be a Treasury obligation.

Mr. Goldsborough. Of course, you have to use your imagination as to what would happen.

Mr. Ford. But imagination does not pay——

Mr. Goldsborough. I know, and I cannot tell you; nobody on earth will tell you the amendments that will be necessary to this legislation in 8 years, and I can only surmise—I won't use the word imagination, but surmise—that when the point was reached where the bank reserves amounted to 100 percent, then all of this money would be validated as money and cease to be interbank currency.

Mr. Ford. Of course, the Treasury has issued it——

Mr. Goldsborough. It amounts to the issuance of money by the Government instead of by the banks.

Mr. Ford. When the bank issues money, it expects to get that money validated later in some way. It is issued on that 10-percent reserve, it is true, but here you are issuing $72,000,000,000.

I am not hostile to the idea; I am merely working the thing out in my own mind, but I am wondering, assuming the maximum, assuming that the country was then on an even keel, production approximately being consumed, because that is the problem, for what we are driving at is some method whereby underconsumption can be cured, but if it can be cured in that way, and we have the country on an even keel, I am wondering if one solution of the problem would not be this, a small gross overturn of business to reimburse the Treasury or its outlet, thereby putting something behind this interbank currency, or the taxing power of the Nation behind the interbank currency, and validating it over a period of years at a certain percentage per year.

Mr. Goldsborough. Mr. Ford, I wonder if I can make myself clearer by illustration. Of course, we hear daily and hourly, and almost every minute, somebody talking about the necessity of balancing the Budget.

Mr. Ford. This has nothing to do with that.

Mr. Goldsborough. Yes; I think it has.

Mr. Transue. Let us hear what Mr. Goldsborough has to say.

Mr. Goldsborough. I am trying to answer your question by an illustration. In other words, the average individual looks upon a debt of one individual to another exactly in the same way as they look upon a debt of society to itself, and I do not think that the cases are analogous at all.

For instance, we will say, and I do not know what the correct figure would be, I just do not remember, but I think that we now have in circulation about $45,000,000,000, against the $62,000,000,000 which we had in 1929.

Now, then, the banks have in capital, surplus, and undivided profits, as I said before, less than $7,000,000,000.

Mr. Ford. That is six to one.

Mr. Goldsborough. Yes. The Government's debt, as I remember it, is now about $40,000,000,000, the so-called Government debt.

Mr. Ford. In round numbers, that is about correct.

Mr. Goldsborough. All right. If we should pass legislation tomorrow which said to the banks, "Gentlemen, hereafter you will have to operate on a 100-percent basis. you have to have dollar for dollar what you lend," we could pay the national debt of forty billion tomorrow and still not have money enough in circulation to transact the business of the country, because we would only have the $40,000,000,000 which we had used to pay the national debt with and the $7,000,000,000 of capital, surplus, and divided profits of the banks.

Mr. Transue. You mean by the issuance of currency for the $40,000,000,000, to pay for those bonds?

Mr. Goldsborough. Yes.

Extravagance is always an evil thing; it undermines human nature, and I am no advocate of it, but all of this talk about the necessity for balancing the Budget is bosh, in my opinion, from start to finish.

Mr. **Ford.** I was not talking about balancing the Budget.

Mr. **Goldsborough.** But you were talking about inflation.

Mr. **Ford.** No; I was not even talking about inflation. I was just wondering how this $72,000,000,000——

Mr. **Goldsborough.** The $72,000,000,000 could be translated from interbank currency into real money. If the banks were on a 100 percent basis, we would not have an inflation 8 years from now, because the country could spend a lot more money then than now.

Mr. **Ford.** This interbank currency is the thing that gets in my craw. Is it a Government obligation, a Treasury obligation, or is it merely a symbol that we are going to use for the transaction of business by which the Government will simply undertake to see that production and consumption are balanced, and in order to bring that out, the Government is willing to go to the extent of 20 percent of that volume with the issuance of interbank currency; and, assuming that $72,000,000,000 were used, and the banks were on a 100-percent basis, there would still be the obligation of the Treasury, would there not?

Mr. **Goldsborough.** The obligation on the part of the Treasury; yes.

Mr. **Ford.** The interbank currency would be a liability of the Treasury, would it not?

Mr. **Goldsborough.** Yes. All that we would have to do is to pass a law and say that it was real money, and if the banks were on a 100-percent reserve basis by that time, we would not have any inflation.

Understand, when I fix the figure of 72 billion, I do not know what it would be.

Mr. **Ford.** It might be only 10.

Mr. **Goldsborough.** Yes.

Mr. **Ford.** But I was just wondering about the character of that particular type of currency, as to——

Mr. **Goldsborough.** Under this bill, as it would go into operation, if it went into operation, it would be an obligation of the Treasury.

Mr. **Kopplemann.** It would be of benefit to the record, and also of interest to the members, if you would give us your understanding of the result of putting consumption and production on an even keel by the allowance of a 15 or 20 percent discount. Would you care to say something on that?

Mr. **Goldsborough.** Yes.

Mr. **Kopplemann.** Just give us your theory.

Mr. **Goldsborough.** Mr. Kopplemann, of course, if a lady went downtown to shop, and she had $5, and she had to have a $5 pair of shoes, and there was a $20-percent discount in operation, she could buy here shoes for $4, and have $1 to buy groceries with, or what not; and the idea of the adjustment is to permit the sale to the consuming public of all that our people can produce, instead of having to destroy milk, fruit, vegetables, and livestock in order to hold up prices when those things are needed by our people if they could get them.

If we are now consuming $65,000,000,000 of producible goods, right now in 1938, and if we could produce 100 billion dollars of goods, provided that we could get them to our people by creating this retail discount, and suppose that we increase the income of the country from 65 billion dollars to 100 billion dollars, and keep the ratio of taxation exactly where it is now, and we are now getting in taxes about 4½ billion dollars a year, and we are spending about 5½ billion dollars; if we could increase our income to 100 billion dollars a year, we could collect 6½ billion dollars in taxes, but in that operation of producing an additional 35 billion dollars' worth of goods, we would release nearly 2 billion dollars paid to people on relief, and put them where they would not be an obligation to society.

Mr. **Kopplemann.** I understand the purpose, but all that I wanted——

Mr. **Goldsborough.** Tell me what it is, and I will try to tell you.

Mr. **Kopplemann.** All that I wanted was for you to prove that this 15 or 20 percent discount will produce these results that we all seek.

Mr. **Goldsborough.** Of course, I have no means of proving it.

Mr. **Kopplemann.** Well, as nearly as you can.

Mr. **Goldsborough.** Of course, if you can lower the price on wanted goods and services to the people, you are doing the same thing as if you increased their wages. It does them just as much good. They get that benefit, and in addition to that, all of society's income is increased.

Why, to me it is appalling to thing, and it certainly is so, that half of our people now do not know where they are going to get their breakfast certainly a month from now. Yet, in the fact of that condition, we are daily deliberately passing legislation which decreases production. I do not mean to say that that legislation is not necessary in this emergency. I know perfectly well—I hope I do; I am old enough to know that much—that even though you know where your goal is, you cannot always steer a straight course.

This bill undertakes to steer a straight course. Maybe you have to go this way and that way and the other way in order to dissipate the inertia of society, but certainly, Mr. Kopplemann, if you can decrease the price of goods at retail to the ultimate consumer, you will increase the buying power, and when you do that you help the consumer, you help the retailer, you help the wholesaler, the manufacturer, and the prime producer.

Now, let us illustrate in another way the popular folklore of our economy. We talk about the balance of trade, foreign trade, and we say that when we send out of this country the good things that we want to a greater extent than we get them back, we have the balance of trade. I say that the other country has the balance of trade, because their people are getting more of our goods than we are getting of theirs. We are, in my judgment, looking at things just backwards in this country—just backwards.

So, if we can create a condition where, instead of having to send our surplus abroad—the present surplus, I mean—we can deliver it to our own people, then this conception of the balance of trade will entirely change.

Mr. **Ford.** Might I make a comment there?

Mr. **Goldsborough.** I wish you would. I need all of the help that I can get.

Mr. **Ford.** All right. That is a philosophy that I have thought of a good deal, but do you not remember that we say that our foreign trade is, in normal times, about 10 percent of our gross production?

Mr. **Goldsborough.** Yes.

Mr. **Ford.** And when it operates, it seems to operate all right, but we have to send a certain amount of goods abroad. I do not care how self-sufficient we are, but we have to have four or five things from abroad that are absolutely essential to our entire economy.

Mr. **Goldsborough.** I have no objection to an even trade. I say, I think you are right as long as we can get an even trade.

Mr. **Ford.** Of course, the balance of trade is an anomaly, because for 25, 30, or 40 years the United States had a favorable balance of trade of 500 million dollars, it was stated, but as a matter of fact we did not have anything of the kind. That balance of trade was chewed up on the other side, because we owed at that time, in interest abroad, from loans that we had made in our early productive days a matter of 150 million dollars. We had what are known as immigrant remittances that amounted to practically the same thing. We paid 75 million dollars a year to foreign shippers for hauling our goods in their ships, and the bulk of our marine insurance at that time was European in character, for we paid the European carriers for that. In addition to that, there are anywhere from 50,000 to 500,000 people who travel annually in Europe, and when I pay a hotel bill in Europe, it is the same as if some American buys goods from London, and, as a matter of fact, every bit of the period while we had the so-called balance of trade of 500 million dollars, we were actually on an even keel.

That did not change until the war. Then Europe had to get money, and it turned over all of the American securities that it held, and over a period of 11 months, we became not a debtor Nation, but a creditor Nation, and, becoming that, we did the silliest thing a nation ever did. We immediately raised our tariff, because we said to those countries, "We want our money," but the minute they brought it to our shores, we stood there with a shotgun and would not let them in.

Outside of a few things, such as tin, rubber, bananas, tungsten, and the other things that we have to get, we do not need anything from abroad, and we used to send them two-thirds of our cotton, 25 or 30 percent of our wheat, 20 percent of our manufactures, and 25 percent of our corn, and through that we got what is known as a favorable balance of trade. That usually was the cotton bill. We usually sold about 500 million dollars of cotton abroad, so that that balance of trade that has gotten into the consciousness of the American people is——

Mr. **Goldsborough.** It is simply folklore.

Mr. **Ford.** It is ridiculous. I do not know whether your bill or any measure that we could pass would enable our people to cure the disease that old Ben Butler said was our trouble, underconsumption and not overproduction, and if we could limit our imports just to the few things we really had to have, you would bring about a Eutopia in the United States very quickly. How long the other countries would stand for it, I do not know, but that is what the situation would be from a theoretical standpoint.

But the fact is that I cannot get through my head—and I suppose that I am as dumb as the average individual—just how that interbank currency will work. I just cannot get a clear conception of that. I might conceivably be somewhat interested in your measure as something desirable to pass, but frankly I cannot see that.

Mr. LUCE. My head is equally as thick in that respect as is Mr. Ford's.

Mr. GOLDSBOROUGH. I never noticed any thickness in the skulls of either one of you.

Mr. LUCE. I am referring to the illustration that you gave, that when a lady bought a $10 pair of shoes for $8, under a 20-percent discount, she had $2 left for the purchase of other things, for you cannot create something out of nothing. If she got $2 more of purchasing power, who lost the $2?

Mr. GOLDSBOROUGH. Well, I would like, with your permission, Mr. Luce——

Mr. LUCE. As I said, you cannot make something out of nothing. If she is $2 better off, somebody is $2 worse off.

Mr. GOLDSBOROUGH. There would not be anybody losing anything, as I conceive it.

Mr. LUCE. Then you have made something out of nothing.

Mr. GOLDSBOROUGH. No; I do not agree with that. The $2 would be utilized to pay for other goods. The $2 would be utilized to bring other goods into being which otherwise would never have been brought into being.

Mr. LUCE. I am not talking about that.

Mr. GOLDSBOROUGH. But you are saying that we are giving something for nothing.

Mr. LUCE. No matter what the ultimate result might be, or how beneficial it might be, for the moment she is $2 better off. Why is it that nobody else is $2 worse off?

Mr. GOLDSBOROUGH. You are asking me a question that it seems to me has no application, and therefore it is impossible to answer it. The only thing that I can say is this, that society is furnishing—not any individual, but society is furnishing that $2, in order to have $2 more of wanted goods distributed to the people.

Mr. LUCE. Do you hold that nobody has incurred any obligation by that transaction?

Mr. GOLDSBOROUGH. Yes; I certainly do. As long as you can bring into being an equivalent amount of wanted goods, why, instead of losing, you are making all the time; you are creating real wealth. I think that very often, due to the symbolism that we use, we confuse money with wealth.

Mr. LUCE. I am speaking of purchasing power.

Mr. GOLDSBOROUGH. I know. You are speaking of purchasing power, and to my mind, the way I see it, instead of taking $2 from somebody, you have added $2 worth of goods to somebody's wealth that they would not have gotten in any other way. That is the way that I see it.

Mr. LUCE. Will this difference of $2 be taken care of by something like a dole?

Mr. GOLDSBOROUGH. There is not a word in this bill which constitutes a dole. You have to have purchasing power in order the get the advantage of the discount, and in order to have the purchasing power, you must toil for it, but it does not involve an unnecessary scarity. That is what we have in this country now. Our scarcity is entirely unnecessary.

Mr. LUCE. You are talking about results, but all that I am saying is, for the moment, if I give you $2, you have $2 and I have nothing.

Mr. **Goldsborough.** Yes; but you do not do it that way. This would be a technique not of any individual, but of society in order to increase goods which society wants and wants to get to its people. It is not an individual transaction, and I think that that is often our danger, in confusing an individual transaction with a transaction which is operated by society for its own benefits, an entirely different process, as I see it.

The **Chairman.** You treat the $2 as an addition to the Nation's medium of exchange, which it is the duty of the Government to supply.

Mr. **Goldsborough.** That is correct.

The **Chairman.** And for which the Government will be compensated by additional national income.

Mr. **Goldsborough.** Real wealth.

The **Chairman.** And, of course, increase the capacity to meet the tax burden.

Mr. **Goldsborough.** Yes.

Mr. **Luce.** Have you not answered my question, by saying that society furnishes the $2?

The **Chairman.** In a sense, I think that is true. I see that matter as you do in that regard, but that phase of this proposed legislation does not disturb me at all, because I see the matter from the viewpoint that it is the duty of the Government to supply a medium of exchange. Here we are in this country, blessed as no other country is blessed in the matter of natural resources and all of the things essential to human happiness. Somebody talked about that the other night, and I did not have the pleasure of hearing him, but he said:

> You people are asleep. It is a case of casting pearls before swine. You have all of the blessings, and you do not know what to do with them. You are throwing them away. You are not living up to your possibilities. God blessed you and made all of these things possible, but you are refusing to utilize them.

There is only one thing that I know about this situation. I do not claim to know much, of course; I am only a layman, but there is one thing that I think I do know, and that every man in this country ought to know, and that is that our problem is a problem of distribution. And I sometimes wonder about the responsibility of this committee in this situation. I am fully convinced that a large part of our difficulties is due to the lack of an adequate medium of exchange in this country, and if that is true the remedy should be supplied by the Committee on Banking and Currency, and not by some other committees of this House who approach the problem from an absolutely fallacious standpoint and apply remedies that we have found do not get the answer.

But I did not mean to begin to talk about this. I only wanted to make the one suggestion.

Mr. **Goldsborough.** I want to supplement what you said in one way, because it is very necessary in order that my point of view may be understood.

Of course, if you simply put out $2 in money that did not result in any wealth, you might have inflation, and as Mr. Luce said, in that case you would have somebody giving somebody $2, but under this bill that $2 operates absolutely for the creation of wealth, because the discount does not come into being until the actual purchase is made, so that you have a guaranty, an absolute guaranty that that $2 will be utilized to create real wealth.

Mr. Reilly. What guaranty have you that the woman who bought the shoes will ever spend that $2? She may have plenty of money and would have bought the shoes without the discount,

Mr. Goldsborough. Of course, Mrs. Jones may put the $2 in her shoe, but Mrs. Society as a whole will spend the $2. I cannot tell you what any given woman will do, but I can tell you that people who are in ordinary circumstances are going to utilize, just as they do now, what they have an opportunity to utilize.

Mr. Reilly. That is why your discount ought to go to the people who will presumably use it. If Du Pont goes and buys an automobile for $2,000, and he gets a 20-percent discount, you have no assurance that you will ever get one dollar for purchasing power from that transaction.

Mr. Goldsborough. Of course, you always have the taxation power to take care of that situation.

The Chairman. As I understand the proposition, Mr. Reilly is not entirely correct, for this reason, that this additional currency would accompany goods purchased in consumption.

Mr. Goldsborough. Absolutely, and be used for no other purpose.

Mr. Kopplemann. Then there is this about it, that that woman who had the $2 is the woman representing all of the women, the vast majority of women, who needs more than the pair of shoes. She is undersupplied, and she uses that $2 to help supply herself with the things that otherwise she might not be able to get.

Mr. Reilly. Very true, but millions of people are situated today with plenty of money.

Mr. Goldsborough. I cannot say millions of people.

The Chairman. Some people have, but the great masses of the people do not have, and if you enlarge their purchasing power, you will bring about an increase in purchasing power.

Mr. Reilly. But not to the extent of the discount. That is why you ought to limit it to the underfed one-third, so that they will use it.

Mr. Gifford. Let me see if we can find where the final liability is on this currency. Of course, the woman does not get the $2. The retailer gets a credit slip for his loss of $2—is that right?

Mr. Goldsborough. Probably that would be the way it would be done.

Mr. Gifford. So he deposits the credit slip, and afterward greenbacks are given for it. It cannot be used by the banks.

Mr. Goldsborough. Sir?

Mr. Gifford. It cannot be used to loan money.

Mr. Goldsborough. Yes; dollar for dollar.

Mr. Gifford. The Government cannot use it for credit purposes. The banks cannot lend to you on that.

Mr. Goldsborough. It would not loan the greenbacks. It would have a right to loan. Its legal capacity would be increased by that amount.

Mr. Gifford. It is a separate account that can be loaned for credit purposes in your bill?

Mr. Goldsborough. Yes.

Mr. **Gifford**. And that money can be used to pay the Federal taxes?

Mr. **Goldsborough**. Yes.

Mr. **Gifford**. Therefore, the money created from gifts pure and simple will be accepted in lieu of other funds to pay Federal revenue so badly needed. Therefore, you reduce the legitimate revenue of the Government to that extent.

Mr. **Goldsborough**. Reduce it?

Mr. **Gifford**. Don't you?

Mr. **Goldsborough**. How would you reduce it? If you can increase the wealth of the country from $65,000,000,000 a year to $100,000,000,000 a year, how are you reducing it?

Mr. **Gifford**. I am talking about a specific thing, not about a general dreamland of things, that we will increase society's wealth. If I am in business and I give away money, and then the Government comes back and says that I can pay my taxes that way, and I am being paid that money that is squandered, that is given away——

Mr. **Goldsborough**. I cannot follow you.

Mr. **Gifford**. As an ultimate thing, the Government has issued greenbacks to make that good. You give away money. We print actual greenbacks that must be redeemed by the Government. If we accept that kind of money for debts, it is not clear to me that it means the proper revenue to clear our obligations. How will the Nation pay its obligations to the bondholders with that kind of money?

There is another question. That index always interested me that you presented to the committee before. When consumption has already kept pace with production on a particular item, you still make this discount on that sort of a purchase. If as many shoes are sold now as can be produced now, you still would pay a discount on that?

Mr. **Goldsborough**. Yes.

Mr. **Gifford**. It would be included in your general index?

Mr. **Goldsborough**. Have to be.

The **Chairman**. Gentlemen, the House is in session, and we shall have to recess until tomorrow morning at 10:30 a. m.

(Thereupon, at 12:02 p. m., an adjournment was taken until Tuesday morning, February 1, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

TUESDAY, FEBRUARY 1, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:48 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Reilly, Mr. Hancock, Mr. Williams, Mr. Spence, Mr. Farley, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKough, Mr. Evans, Mr. Transue, Mr. Fish, Mr. Luce, and Mr. Crawford.

The Chairman. The committee will come to order, please.

Mr. Goldsborough, you may proceed in your own way.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND—Resumed

Mr. Goldsborough. Thank you, sir.

Mr. Chairman, there were a great many interesting inquiries yesterday which I will endeavor to answer today insofar as I am capable of doing so. Before doing so, however, I want to make a comment upon what I said yesterday regarding the new housing legislation, the conference report on which is now being acted upon in the Senate.

I do not want to be understood as opposing that legislation, because, as a matter of fact, that legislation has been extremely useful in many ways. I know that nothing else has done as much to improve the technique in the policies affecting the treatment of the public by private lending institutions as has the housing legislation which has been passed by the Congress. You all may know as much about the methods of lending institutions as I do. For instance, they do this sort of thing: An organization would be set up as a title company, and the same stockholders and the same directors would set themselves up as a building concern, and they would set themselves up as a bonding company, and when an application was made to them for money, the first thing they would do would be to charge a commission for lending the money, and then they would charge a fee, the same group of men, but under a different corporate organization, for searching the title, and then they would charge a fee for furnishing a bond to themselves—that is what it amounted to—and then they would charge a fee for preparing the papers, and they would make from 23 to 25 percent before they got through with a customer.

This housing legislation has done away with all of that vicious practice, and if it had done nothing else but that, it would have rendered a tremendous public service.

Then it has done another thing, in my opinion. This housing legislation has helped the people to have a consciousness that this matter of debt should be minimized as much as possible, that the burden of debt should be made as light as possible. So that, far from being opposed to the legislation, I am in favor of the legislation. Of course, I supported it—you all understand that—but I was using it yesterday to simply illustrate the fact that if you can put your buying power in at the bottom, then the individual can accumulate his own money and build his own house and render to a large extent the accumulation of debt under our present system unnecessary.

Mr. **Ford**. Would the gentleman yield for an observation?

Mr. **Goldsborough**. Yes.

Mr. **Ford**. In enumerating the things that the corporations used to do and that they have cut out, you left out one very important thing, and that is that every 3 years the loan came due, and they would then have to go through the same process over again.

Mr. **Goldsborough**. Yes. That was another part of the same racket.

Mr. **Ford**. "Racket" is right.

Mr. **Goldsborough**. Now, on yesterday the gentleman from Massachusetts, Mr. Luce, made the observation that if the typical woman who went to the store to buy a pair of $10 shoes, where there was a 20-percent discount, bought the shoes for $8, someone would have to lose the $2.

That is a fair statement, is it not, Mr. Luce?

Mr. **Luce**. All right.

Mr. **Goldsborough**. That somebody would have to lose the $2, and that in his opinion that was economically unsound and not defensible, and fostered indigence and laziness and things of that kind.

Now, then, without meaning to indulge in satire or sarcasm, Mr. Luce, because there is nobody on this committee on either side that missed you as much as I did in the 2 years that you were not with us, and whenever I look around and find you here, it is very helpful to me; but it is true, it seems to me, that things that we have been used to all our lives we lose sight of. For 100 years New England has been receiving a subsidy in the shape of a tariff which has been paid for by every consumer in this country, and because of habit, and because you are used to it, apparently you have lost sight of that fact, and you do not disapprove of it. You think it was sound. You do not think that it has made for inefficiency among the manufacturers of New England. You think that it has helped New England, and the balance of the country.

What we are proposing by this bill is to subsidize the manufacturers not only of New England but elsewhere, and to subsidize the farmers of the East and West, and to subsidize every consumer in this country equally. That is the only distinction that I can see between the thing that you are accustomed to and what is suggested in this bill. If that is not a fair statement, I wish that you would remind me of it, because I am very sincere in what I have said.

Mr. **Luce**. May I say that this proposal of yours is one of a group of proposals that have much in common—for instance, the Townsend plan. I am not one of those inclined to scoff or reject the Townsend plan offhand. I want to think it through, and find out where the flaw is in it, and I have put a good many hours into trying to think it through, the same way that I am trying to think through your plan. So my question was directed merely to finding out——

Mr. **Goldsborough**. I am fully aware that your questions are sincere; there is no doubt about that in my mind. I did not mean to question that in any way.

Mr. **Luce**. I have been thinking it over again since I talked to you yesterday, trying to think it through and find out who would bear the ultimate burden of a transaction of that sort. If it is just, I want to be for it. If it is not just, I want to be against it, and my questions are aimed solely to enable me to think the matter through.

Mr. **Goldsborough**. I am certain of that.

Now, Mr. Ford, we had a discussion yesterday in which you observed that the operation of this so-called interbank currency was not clear to you, that you did not see exactly what it was. If you will permit me, I would like to give you my conception of it, not that it is any better than yours, but simply to explain my conception of what it is.

The only reason that it is made interbank currency in this bill, instead of making it money that goes directly to the banks, is this, that in drawing this bill, as I attempted to explain in the last session in the long discussion which I made, in the written material which I had, the attempt was made to put this bill into operation without disturbing the workings of the present banking system, which is a fractional reserve system.

Now, then, if this interbank currency, instead of being interbank currency, were paid directly to the banks as deposits, it would so increase the reserves of the banks as to cause a tremendous inflation as long as we operate the present banking system; so, in order to make it possible for the present banking system to continue its operations without interference of any kind or character, I thought it better to simply make this money interbank money, and provide that it only could be used as a 100-percent reserve, instead of mixing it with the other funds of the bank where it could be used as fractional reserves, and thus creating an impossible situation.

Is that helpful insofar as my explanation is concerned?

Mr. **Ford**. Well, I do not believe that at any time I have had any misapprehension as to what the money was going to be used for, but the purpose of my inquiry, and what I am still a little bit hazy on, is this, that after this interbank currency is issued by the Treasury, and let us take any figure—one billion, or two billion, or five billion—when the discount is operating, and we will say that it is on a 15-percent basis, and when there is this deficiency amounting to $3,000,000,000, the difference between what the merchants got for their goods and what the banks credited them with, naturally the United States Treasury issued to the banks $3,000,000,000, in interbank currency that they could use to settle their balances between themselves.

Mr. **Goldsborough**. Also as 100-percent reserves.

Mr. **Ford**. I think there was some statement made, too, that they could use that for taxes.

Mr. GOLDSBOROUGH. They could use it for taxes, and in case they are in need of cash, they could get the cash.

Mr. FORD. In that case, it is a direct obligation of the United States Treasury to the extent of the amount issued, is it not?

Mr. GOLDSBOROUGH. Yes.

Mr. FORD. Now, we will say that here is one of the largest banks, operating on a big scale, that has $5,000,000 of that interbank currency in their reserve, and a contingency comes up when they are called upon for a lot of money.

Mr. GOLDSBOROUGH. Cash.

Mr. FORD. Real cash. They cannot use that reserve in that case, can they?

Mr. GOLDSBOROUGH. Yes. They can get the cash if they have a demand for it from their customers. The bill specifically provides for that, that if there was a run on the bank or anything of that kind, they can get the cash.

Mr. FORD. But the minute they use that reserve in the normal, current business, it becomes a part of the currency of our money economy of the United States.

Mr. GOLDSBOROUGH. That is correct.

Mr. FORD. Then isn't this merely—and I do not mean this in any harsh way—isn't that merely injecting Treasury money into the currency flow in a rather subtle way, without saying so?

Mr. GOLDSBOROUGH. That is a fair statement on your part, but——

Mr. FORD. As I said, I am merely asking for information.

Mr. GOLDSBOROUGH. That is a perfectly fair statement, but it is being done without interrupting or interfering in any way with the normal functions and the normal operations of a bank.

Mr. FORD. Let me make this observation. The general assumption or presumption is that if the United States Treasury issued a lot of fiat currency it would immediately create a policy of distrust and possibly of inflation, whereas by the method you are suggesting it might be subtly injected in there without anybody paying very much attention to it. The bank could put that in their reserves and later on it would quietly slip into general circulation, and the general circulating media of the country would be increased to an extent where the flow of money and the flow of goods would be what we would presume to be a general cycle of prosperity, but all of that time there is still the obligation that the banks are indebted to the Treasury to the extent of $3,000,000,000, and although nobody seems to know anything about it, will that ever go to the banks? Is there any method whereby it can get back?

Mr. GOLDSBOROUGH. The answer to that is this, that insofar as this bill is concerned, the method provided is that if the price level should rise and the Federal Credit Commission should reach the conclusion that there was more money going into circulation than the increased supply of goods justified, in other words, that money was increasing faster than goods, then they have the right to call the interbank currency in by requiring the banks to call some of their loans. The bill specifically provides for that.

Mr. FORD. Would that be——

Mr. GOLDSBOROUGH. I will tell you what I did, Mr. Ford. I deliberately left out of this bill any specific statement about taxation. The reason I did that is because taxation can be used without this bill, and to interject anything into the bill which would make the powerful interests think that their taxes were going to be increased might unjustly and detrimentally affect the bill, and when I say unjustly, I will try to explain what I mean.

Let us assume, for the sake of argument, that we are getting an income in this country of about $60,000,000,000 a year, and that it requires $100,000,000,000 to produce the maximum amount of prosperity without inflation, and suppose that we are able to inject into the monetary system by virtue of this price discount sufficient money to raise the income of the country from $60,000,000,000 to $100,000,000,000.

Now, the only additional tax that would have to be levied would not be a tax to support the $60,000,000,000, because it would not require any increased tax to support that, and the tax on the $60,000,000,000 would be decreased because some two or three billion dollars of taxes which now go to relief would be unnecessary, and, in addition to that, those who bear the heavy burden of the income tax would get a very considerable part of the extra $40,000,000,000, because, naturally, under a profit system, under a capitalistic system, as money goes into the bottom and profits begin to accumulate, that money gradually gets to the top and those at the top get the largest amount of benefit from it.

So I did not think it was necessary to interject a specific method of taxation into the bill, because the tax system is perfectly able to take care of itself without injecting any specific clause of that kind into a monetary bill.

That is as frank as I can make it.

Mr. **Ford**. Is this a fair observation, on the basis of your theory, that if the injection of this interbank currency into the system ultimately raised the income of the country from $60,000,000,000 to $100,000,000,000, the tax base necessarily would be broadened in order to collect the $7,000,000,000 that we need at the present time, and instead of having to tax as much as 75 percent in some spots, we could cut that to 35 or 40 percent because of the larger base to go on, and as a matter of fact we would not have to collect so much in taxes from each individual. We could collect less. So it would operate, according to your theory, as a tax reducer, more so than it would operate as a tax increaser?

Mr. **Goldsborough**. That is my theory; yes, sir. You have stated it fairly.

Mr. **Ford**. Another theory has been proposed before the Ways and Means Committee, and that is to take most of the taxes of the large holdings and put them in the form of a manufacturer's tax, and therefore release that money that is driven out of industry by reason of the heavy taxation put on it and it would flow freely and bring about the same end.

I look on that particular theory as I do upon what we used to call the trickle theory, which is that when a lot of fellows above make the money, it trickles down so that the fellows below get some of it, but you have a system that looks like the reverse of it.

Mr. **Goldsborough**. I hope that it is the reverse of it.

Mr. **Ford**. Although it accomplishes the same thing in the end.

Mr. **Goldsborough**. If it accomplishes the same thing, I would just as soon have the trickle theory as this one.

Mr. **Ford**. It would accomplish it to this extent, that they would pay less taxes because of the larger volume of business done, and the theory of taxation of the business of the country is merely for the purpose of operating the Government. That is true, is it not?

Mr. **Goldsborough**. That is true, and I have tried to make a study of the capitalistic system and the profit-making system as contradistinguished from any other system of government, and I have reached this conclusion, that in the first place I want to maintain the capitalistic system. In the second place, I want to maintain the profit system. I have reached the conclusion that under those systems all money that is put into society of necessity has, first one profit and then another, that is added to the cost of the article, so that the money gradually goes up to the top. Now, then, the only way on earth, after you have reached a certain point in putting the money on the market, that you can supplement that buying power is to take some fom the top and put it in again, and start the process all over again, and it does as much good to the man at the top as the man at the bottom, for if we cannot distribute what he can produce, the wealth of the man at the top is decreased, so that he is better off if some of that is taken by taxation and put at the bottom.

Mr. **Ford**. I have given this bill a great deal of thought, and I have weighed very carefully the various theories which have been propounded in this and other proposals for the solution of the problems which face us at the present time. I have had dozens of those theories presented to me, but if seems to me that as long as we are going to maintain a capitalistic system, we have to provide that the three-legged kitty that I referred to a while ago, when we were speaking on another subject off of the record, is sufficiently fed so as to keep her going.

Mr. **Goldsborough**. Do you not think that it has to be fed from the bottom?

Mr. **Ford**. Production is the bottom. That is where it gets its milk.

Mr. **Goldsborough**. If you feed production instead of feeding consumption, you are not giving production any chance to distribute what it produces, but if you put the money in at the bottom, it goes clear through the system, and it seems to me that that is the way this thing would work in practice after it got going. I do not think that it would then have to be used very much. I think that just as soon as business understood that when business began to slump, there would always be this discount which would stimulate buying power on the part of the consumer, it would increase the confidence of industry to an extent certainly that we have not experienced for years past, because just as soon as industry realized that we had a system which would stimulate buying power whenever buying power got slack, it would invite industry to figure ahead. They could tell what they should buy, and what they could afford to borrow and put on their shelves, and I do not think that this system would have to be used very much.

Mr. FORD. There is a temporary system of amelioration in that particular being practiced by all of the great department stores. In August or July, or at various times, they will sell a regular $39.75 woman's dress for $22.50, or something like that. They do that right along. They give a discount, and the women flock there to buy.

The same is true of almost every line of retail trade. They have great bargains on various days, and to that extent they stimulate the shift between what is now on their shelves and the new stuff.

But there is no compensating return for the discount that they have given. They have to take the rap themselves, and take it out of previous profits. Where they sell a dress for $22.50 that they previously sold for $39.75, they are making less profit, but what you are aiming to do is to make that kind of business unnecessary, to establish a general discount rate over the Nation, a discount rate that will be governed by the board's findings as to the condition of production and consumption, keeping them in something like a stabilized or level condition.

Mr. GOLDSBOROUGH. That is true.

Mr. FORD. Whether or not the mechanism that you would employ in this bill would accomplish that is a broad question.

Mr. GOLDSBOROUGH. Exceedingly so.

Mr. FORD. We all realize it, and I hope that I have not taken too much time, but I was trying to get this thing into my head.

Mr. LUCE. Mr. Ford, do you understand this proposal to be one for temporary use?

Mr. FORD. No; but a permanent policy, to stabilize and bring together production and consumption over a long period of years.

Mr. LUCE. This seems to be quite important, and I had the impression that Mr. Goldsborough contemplated continuing the plan, which would work all the time.

Mr. GOLDSBOROUGH. That is correct.

Mr. LUCE. But the illustration that you gave, Mr. Ford, of a marked-down sale is purely one covering a temporary condition.

Mr. FORD. The retail business has employed that device as long as I can remember.

Mr. LUCE. Oh, yes; but it operates only certain times of the year.

Mr. FORD. Yes.

Mr. LUCE. It does not go right through the year.

Mr. FORD. I say that in a limited way that device is being used by the retail business at the present time, but only in a limited way. Under Mr. Goldsborough's bill, the periods might come where production and consumption are level, and in that case——

Mr. GOLDSBOROUGH. We would not use it at all.

Mr. LUCE. How can you suspend it?

Mr. GOLDSBOROUGH. We will suspend it when the Federal Commission finds that consumption is approaching the limit of production by 15 percent. Then you would cease to use it entirely.

Mr. LUCE. I did not understand that.

Mr. GOLDSBOROUGH. That is correct.

The CHAIRMAN. That is in the bill.

Mr. GOLDSBOROUGH. Now, Mr. Chairman, Mr. Reilly suggested yesterday that if a measure of this kind were adopted, it should not be universal, but should go to a selected class, those would be pretty certain to use the discount.

I wonder if it would be interesting to quote from a finding made by the Brookings Institution, in a work entitled "Income and Economic Progress," pages 37 and 38:

> First, the consumptive requirements or wants of the people were far from satisfied during the period of our highest economic achievement. The value of the total national production of goods and services in 1929, if divided equally among the entire population, would have given to each person approximately $665. There were nearly 6,000,000 families with incomes less than $1,000; 12,000,000 with incomes under $1,500; over 16,000,000 with incomes under $2,000; and over 19,000,000, or 71 percent of the total, with incomes less than $2,500. A family income of $2,500, at 1929 prices, was a very moderate one, permitting few of the luxuries of life. Hence it was clear that the consumptive requirements, and especially the wants, of the masses of the people were far from satisfied.
>
> To raise the incomes of the 194,000,000 families receiving less than $2,500 in 1929 to a $2,500 level, with no changes in the incomes of the families receiving more than that amount, would have required an increase in national production of more than $16,000,000,000. A horizontal increase of $1,000 in the income of all families receiving less than $5,000 in 1929 would necessitate an expansion of production to the extent of over $25,000,000,000. To give all the families of the Nation a reasonable standard of living, such as is set forth in studies made by the Bureau of Home Economics of the United States Department of Agriculture, would have necessitated an increase in production over 1929 levels of approximately 75 percent. The full utilization of our productive capacity, it will be recalled, would have permitted an increase in production of only about 20 percent, or $15,000,000,000.

This was written several years ago—

> We were clearly not confronted in 1929 with overproduction, either actual or potential. The desires of the people were vastly greater than could have been satisfied by the productive power then available.
>
> Second, the market demand for consumption goods was less than our capacity to supply such demand. That is to say, while we could not have supplied all of the goods that were desired by the people, we were able to furnish a larger volume than the people were willing or able to purchase with the incomes which they had available. A substantially greater output of consumption goods would undoubtedly have resulted had the market demands of consumers been larger.

Mr. Luce. Will you permit me, right there, for the sake of the record, in order that whoever may read it may not get confused, to say that those figures—and I have read that—contain a confusing element often found in quotations from the Brookings Institution and others, in that they start out with a per capita figure and jump then to a family figure, without calling the attention of the reader to that fact.

I do no contest any single figure there, but I think that the Brookings Institution would have done better if they had pointed out that part of their figures are on a per capita basis and part on a per-family basis. The average family of four people—and sometimes four and a half is referred to as constituting the average family—has three workers in it, so that you have to be on your watch all the time in drawing inferences from those and other like quotations.

That is solely for the record.

Mr. Goldsborough. Yes, sir; but I think it is fair to call the attention of the committee to the fact, which of course all members of the committee are as well aware of as I am, or more so, that the

Brookings Institution is a very conservative organization, that it is understood to be a conservative organization, and that therefore we can safely reach the conclusion that they have not overstated the case. The natural inference would be that a statement of theirs was an understatement rather than an overstatement.

I only thought that that might be of interest to Mr. Reilly in connection with his observation yesterday.

Mr. **Reilly.** I want to make this observation, that in 1929, when those statistics were applicable, as you say, we had 50,000,000 people who had bank deposits, and if they got that 20 percent more, they would have put it right back in the banks where they had the money.

(Thereupon, the committee, at 12 noon, took an adjournment until Wednesday morning, February 2, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

WEDNESDAY, FEBRUARY 2, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:55 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Kopplemann, Mr. Ford, Mr. Brown, Mr. Patman, Mr. Evans, Mr. Transue, Mr. Barry, Mr. Gifford, Mr. Luce, and Mr. Crawford.

The **Chairman**. Mr. Goldsborough, you may resume your statement.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND—Resumed

Mr. **Goldsborough**. Thank you, sir.

Mr. **Patman**. Mr. Chairman, may I ask him some questions now?

The **Chairman**. Certainly.

Mr. **Patman**. Mr. Goldsborough, I have been giving serious consideration to this bill. When I discovered that the chairman was determined, and you were determined, to fully complete the hearing, I thought there was a determination on the part of the chairman and yourself to get a favorable report on this bill, so I have been giving it very careful consideration.

I thoroughly agree with you that we should have some distribution of purchasing power. I would go to any extent to distribute purchasing power among the masses. There is no difference of opinion between us on that, but the mechanics of this bill appear to me to be absolutely impossible, if I understand it right, and that is why I want to ask you some questions.

First, if I understand the bill right, every retailer in this country would first have to get a license from the Federal Government to operate, before he could make any sales of any kind. This bill includes everything that is sold to the consumers at retail. It includes everything from an article dispensed at a soda fountain——

Mr. **Goldsborough**. Is this a question, or a statement?

Mr. **Patman**. I am going to ask a question, but I wanted to make a statement to preface my question.

It includes everything sold from a package of pins to a locomotive.

Mr. **Goldsborough**. Not a locomotive, because a locomotive would never be sold to an individual, a natural person.

Mr. Patman. It is possible that Henry Ford might buy one, and if he did——

Mr. Goldsborough. I do not think that that is an illustration at all.

Mr. Patman. We will say that everything that is bought by persons, not corporations——

Mr. Goldsborough. By natural persons.

Mr. Patman. On everything that is bought by natural persons under this bill, if it becomes a law, automatically there will be a 15 percent retail discount. That means that if I go down here to the store and purchase $10 worth, I will have to pay only $8.50. That other $1.50 I will necessarily have to sign some kind of a voucher for, because I did not pay it.

Mr. Goldsborough. No; that would not be the mechanics of it.

Mr. Patman. What would be the mechanics? What would I actually do?

Mr. Goldsborough. All you would do would be to pay $8.50 for the shoes, if that was what you were buying, and then go right on home.

Mr. Patman. Then that would be left up to the retailer?

Mr. Goldsborough. Yes.

Mr. Patman. And I would not have to do a thing?

Mr. Goldsborough. That is correct.

Mr. Patman. The retailer then would write out a statement of some kind, or a voucher, would he not?

Mr. Goldsborough. Well, now, it would take someone who is more familiar with how those things are done in practice than I am in order to tell you that. Anyone who has administered, for instance, the retail sales tax, such as they have in New York City, which applies to everything that is sold at retail, could answer that. There are some mechanics whereby the retailer settles with the State of New York, and it is done with very great accuracy, I understand.

Mr. Patman. Undoubtedly it is, but——

Mr. Goldsborough. Just how they go about it, I do not know, but it would not be more difficult, in my opinion, for the retailer to settle with the bank——

Mr. Patman. We will say that we do not know how that will be done, but that something will have to be done; that this local retailer will have to take a statement or a voucher or something to his bank.

Mr. Goldsborough. There is no doubt about that.

Mr. Patman. Something will have to be done?

Mr. Goldsborough. That is correct.

Mr. Patman. And the retailer takes that to his banker, and his banker is compelled, under this bill, under penalty, to give him credit for that $1.50?

Mr. Goldsborough. That is correct.

Mr. Patman. Then this banker has issued to him, to compensate him for it, what is known as interbank currency, that will be issued by a commission here in Washington, and that will be in the form of greenbacks or something like that?

Mr. Goldsborough. Well, I would not think so. I would think he would simply get a credit, just like he gives his customer——

Mr. Patman. Now, then——

Mr. Goldsborough. And under this bill, if he needs the cash, if he gets a run on his bank, he can get it.

Mr. **Patman**. This bill calls, right off, for $10,000,000,000 of that currency to be issued?

Mr. **Goldsborough**. Yes, sir.

Mr. **Patman**. Therefore something physical will have to be issued?

Mr. **Goldsborough**. It would, if it was needed.

Mr. **Patman**. $10,000,000,000 of it would have to be issued right off?

Mr. **Goldsborough**. I did not say that it would have to be issued right off. I said the money would have to be available if needed.

Mr. **Patman**. I thought the bill said that.

Mr. **Goldsborough**. No.

Mr. **Patman**. It provides that the total amount of the initial currency shall not exceed $10,000,000,000——

Mr. **Goldsborough**. That is right.

Mr. **Patman**. Maybe I was wrong on that, but it will be issued up to $10,000,000,000, and the point that I would like to ask about is this: As it is, it includes everything in the food-store line—eggs, poultry, baker's goods, candy, delicatessen articles, fish, and the products of meat markets, and of all food stores. It includes merchandise like that handled in the department stores. It includes automobiles. It includes the products of filling stations, furniture, lumber, building materials, hardware, and it even includes rents?

Mr. **Goldsborough**. Yes.

Mr. **Patman**. Then it takes in the eating and drinking places, drug stores, beer and liquor stores, and all other retail stores, including second-hand stores.

Let us say that this law is in effect, and these million and a half retailers are all honest men, but sometimes they are not honest. As evidence of the fact that we do not have honest people in these places of trust, out of 30,000 fourth-class postmasters in America today, 6,000 of them are under indictment by the Post Office Department for falsifying their accounts. That is a matter of record right down here. That is not generally known, but it is a fact, that 6,000 of them out of 30,000 have been accused of padding cancelations——

Mr. **Goldsborough**. You said that they were under indictment.

Mr. **Patman**. I said that the Post Office Department indicted them.

Mr. **Goldsborough**. I did not so understand you. I understood you to say that they were indicted.

Mr. **Patman**. They are indicted by the Post Office Department; in other words, they are accused, and the Post Office Department has what they consider absolute proof that they have been falsifying their accounts.

Mr. **Goldsborough**. It is very strange that they are allowed to stay in office. You could not get the Post Office Department to make the statement that you are making.

Mr. **Patman**. Well, I got my information from the Post Office Department, so that there cannot be any question about that, and I know what I am talking about on that.

Mr. **Goldsborough**. That is 1 out of 5, and that just simply cannot be accurate.

Mr. **Patman**. All right. Let us say that there is 1 out of 10, if you want to, but we know that there are a certain number doing that.

Mr. **Goldsborough**. I have 500 of them in my district, including fourth-class postmasters, but there has not been that difficulty in my district.

Mr. Patman. They are all honest in your district. Some districts in this country have all the honest ones.

Now, then, if it happened that way in the Post Office Department, certainly out of a million and a half retailers you will find some dishonest ones, and suppose——

Mr. Goldsborough. That is your statement, you know, and not mine.

Mr. Patman. I am asking you to answer it, because I feel like——

Mr. Goldsborough. The question is, It is all right with me for you to make a statement, but don't make it in such a way to indicate that I am making it.

Mr. Patman. That is in the record now, because what I say will be my responsibility.

Now, here are a million and a half retailers that have got a blank check on Uncle Sam. Anybody can go in and buy anything that they want to, an automobile for $1,000, or an automobile for $5,000 or $10,000, and they give the one who buys it a 15-percent discount.

Mr. Goldsborough. Don't you think that what you ought to do, and you have the privilege of doing it, is to simply be a witness against this bill? What you are doing now is simply testifying, giving opinions.

Mr. Patman. I want to ask you questions, because I might be wrong about this, and I want to be set straight.

Mr. Goldsborough. You have the privilege of testifying before this committee.

Mr. Patman. But what I would like to ask you is, won't you have to have some supervision over this, to carefully watch all of these people, to see if they are going to defraud the Government?

Mr. Goldsborough. That is self-evident.

Mr. Patman. It takes a large number of people to supervise the post offices, and it certainly will take a much larger number to supervise all of these people.

Mr. Goldsborough. That is your statement.

Mr. Patman. You know it well.

Mr. Goldsborough. No; I don't know anything of the kind. I know this, that it won't be any more difficult to enforce this law than it will be to collect universally a retail sales tax, not a bit, and the same formula used for the purpose of collection a sales tax readily can be used to collect this 15 percent.

Mr. Patman. Suppose that a farmer in your district had a couple of tons of hay, and you wanted to buy it. If you bought it from him directly, you could not get any discount, but if he sells it to the retailer, and the retailer sells it to you, you would have a 15-percent discount.

Mr. Goldsborough. He has to be a retailer——

Mr. Patman. In other words——

Mr. Goldsborough (continuing). Who procures a license and sells to the ultimate consumer.

Mr. Patman. That will force——

Mr. Goldsborough. If he is not a retailer, he cannot get a license and cannot get a discount.

Mr. Patman. Therefore that will force all business to be done through retailers.

Mr. Goldsborough. I do not know that it will; no.

Mr. Patman. How could you afford to buy a dozen eggs directly from a farmer, or a ton of hay, where you would not get any discount, whereas if you bought it from the retailer you would get a 15-percent discount? It is obvious that all business would be forced through these retailers.

Mr. Goldsborough. I do not think so.

Mr. Patman. Now, then, suppose that I go to a retailer and I buy a car for $1,000——

Mr. Goldsborough. As a matter of fact, I make this statement, that in the State of New York, for instance, a man who sells a ton of hay to someone does not pay any sales tax.

Mr. Patman. Suppose that I buy this $1,000 car, and get a $150 discount, and the merchant gets credit from the Government, and then I sell it right back to the merchant and he sells it to somebody else, and gets another $150 discount; wouldn't it open all kinds of room for dishonest dealings along that line, which the Government would find almost impossible to check up on?

Mr. Goldsborough. You know as well as I do that we have to correct the income-tax law at every session of Congress in order to try to stop fraud. It is perfectly evident that there would be just as many attempts at fraud in connection with the operation of this bill as there would be in connection with the operation of any legislation.

Mr. Patman. That is right.

Mr. Goldsborough. There cannot be any dispute about that.

Mr. Patman. Every sale would have to be checked.

Mr. Goldsborough. No; of course not.

Mr. Patman. Suppose that you are the head of a corporation, and as president of the corporation you want to buy an automobile.

Mr. Goldsborough. For yourself?

Mr. Patman. No; for the company.

Mr. Goldsborough. Then you cannot get the discount.

Mr. Patman. Suppose that you are the president of this company, and you want to buy a $1,000 car. If you go to buy that for the company, you would have to pay $1,000, but if you got some friend of yours to buy it—which, of course, you would not do, but I am giving an illustration—he would get the 15-percent discount, and then he would sell it to the corporation.

Mr. Goldsborough. Of course, my only answer to that is that when this bill is passed, there will be just as many crooks in this country as before. This bill is not going to make either more or less crooks.

Mr. Patman. But won't it make a rather productive field?

Mr. Goldsborough. I do not think so; no. I think that after it has been in operation a little while they could check up with almost absolute accuracy as to whether or not——

Mr. Patman. Now, everything that the corporation bought would be at full price?

Mr. Goldsborough. Yes.

Mr. Patman. It just occurs to me that it would take a lot of people to check up on these corporations. There would be such a great incentive for the individuals to buy everything for the corporation and get the 15-percent discount and handle it in some way so that the corporation would not have to pay full price that it occurs to me that it would be almost an impossible thing to supervise that.

Mr. Goldsborough. You are testifying now.

Mr. Patman. I understand. Now, this applies also to passenger transportation, like on the railroads, and freight, and gas and electricity, and rents, and hospitalization, and schools, and theater tickets, everything.

Mr. Goldsborough. What about schools? What do you mean?

Mr. Patman. You have schools in here—services. That is, if I sent my boy to Staunton, Va., to the military school, and it cost so many hundreds of dollars a year, I would get a 15-percent discount on that, would I not?

Mr. Goldsborough. That is correct.

Mr. Patman. And everything in regard to hospitalization and schools—everything would get that 15-percent discount.

Mr. Goldsborough. But, as a member of this committee, if there is any item in there you do not approve of, you have the opportunity to proffer an amendment to perfect the bill.

Mr. Patman. If I can find something in this to build on, I will work with you, if I think it can be perfected, and that is the reason I want to ask you these questions.

So the law automatically places the 15-percent discount into effect.

Now, then, the point is, when a billion dollars, we will say, of these certificates have come in, and, of course, it will take no time for a billion dollars' worth of interbank currency to pile up, who is liable for that interbank currency? Whose obligation is it? It must be the obligation of someone.

Mr. Goldsborough. Well, I may not understand your question, because the answer to me is so obvious. The Government would be responsible.

Mr. Patman. The Government would be responsible?

Mr. Goldsborough. Yes.

Mr. Patman. It is an I O U of the Government?

Mr. Goldsborough. Yes; through the Federal Credit Commission, as set up by this bill.

Mr. Patman. Suppose that I do not have the money to pay my taxes, and I have to go to my bank to borrow $500 to pay my taxes, cannot the bank use interbank currency to pay those taxes?

Mr. Goldsborough. To pay your taxes?

Mr. Patman. Yes.

Mr. Goldsborough. Well, the bank would not be paying your taxes.

Mr. Patman. Oh, yes. I am borrowing the money from them. They pay the taxes, and I give a note for it.

Mr. Goldsborough. I do not understand that the bank would do that. I should think that you would give your own check for your taxes, would you not?

Mr. Patman. Why wouldn't the interbank currency be good for the payment of taxes? It is a Government obligation, money that the Government said was good and would accept in payment of the bank's taxes.

Mr. Goldsborough. I do not——

Mr. Patman. Why should not they pay anybody's taxes with it?

Mr. Goldsborough. The answer, to my mind, would be obvious. I do not know whether you were here when Mr. Ford and I discussed that matter yesterday of interbank currency. The only purpose of making that interbank currency not available except in a bank emergency is to prevent its getting into the reserves and increasing the reserves of the banks and causing inflation. That is the only purpose. It would be perfectly all right to pay the cash to the bank——

Mr. Patman. You would be in favor of that?

Mr. Goldsborough. Except that I did not want to disturb the present banking system, and in order not to disturb it, I segregate this fund and prevent it from going into the reserves of the banks.

Mr. Patman. Why permit the banks to use it to pay taxes and not let everybody else use it to pay taxes? It is an IOU of the Government.

Mr. Goldsborough. If you think it is a mistake to have that in the bill, we would probably agree to an amendment to eliminate it. It is not a tremendously material matter.

Mr. Patman. Would you agree to that, Mr. Goldsborough, to make all taxes to the Federal Government payable in interbank currency?

Mr. Goldsborough. But the interbank currency does not go to individuals.

Mr. Patman. I know, but the individuals pay their taxes through banks, you know.

Mr. Goldsborough. No; I don't know any such thing.

Mr. Patman. Why shouldn't they be privileged to do that? That is a Government IOU. The Government puts it out, and if the Government says it is good——

Mr. Goldsborough. I am just not bright enough to follow you. That is my difficulty.

Mr. Patman. I appreciate the compliment.

Mr. Goldsborough. Your suggestion simply involves destroying this bill. If you are going to take this interbank currency and make it like any other currency, that simply means to dump the 10 billion dollars in the market and destroy the bill.

Mr. Patman. I am seeking information. You understand it, and I do not.

Mr. Goldsborough. If you understand it, I certainly do not. There is not any question about that.

Mr. Patman. Suppose that we leave it like this, that we will not put it in circulation, but use it to pay taxes. Will you agree to an amendment like that, not to put it in circulation, but leave it exactly as you have it, and provide that this interbank currency may be used to pay any taxes due to the Federal Government?

Mr. Goldsborough. That question to me is so far fetched that I do not know what you are getting at. You may have something in the back of your mind that I do not understand. I do not know the purpose of the question.

Mr. Patman. You know that the Government's IOU should be worth 100 cents on the dollar, and you say that this is a Government obligation.

Mr. Goldsborough. But that is not the issue in this bill. The issue is whether or not it is wise for the Government to provide, when necessary, to the ultimate consumers, a discount on goods sold at retail. That is the issue in this bill.

Mr. Patman. To a natural person, and not a corporation.

Mr. Goldsborough. No; you are going off on the question of whether or not——

Mr. Patman. I know, but the question——

Mr. **Ford**. Just one observation there.

I think that what Mr. Patman is trying to ask is this: What he wants to do is to validate this interbank currency for taxes, public and private, therefore making it——

Mr. **Patman**. Due to the Federal Government.

Mr. **Ford**. Therefore making it regular money.

Mr. **Goldsborough**. As I said before, if a thing like that is done, it simply destroys the theory of this proposed legislation.

Mr. **Patman**. If you let the banks pay their taxes that way, why not let other people pay them?

Mr. **Goldsborough**. It is for the convenience of the banks. It is one of the emoluments that the bank gets for handling this interbank currency.

Mr. **Patman**. They get a service charge.

Mr. **Goldsborough**. The bill also provides for a service charge. That is simply one means of assisting the banks, or recompensing them for granting this service to the public.

Mr. **Patman**. Let me use your illustration. The other day you said that the total retail sales last year were approximately 4 billion dollars.

Mr. **Goldsborough**. No; 40 billion dollars.

Mr. **Patman**. I meant that; not including certain things that this bill includes.

Mr. **Goldsborough**. That is, public utilities, such as electricity, telephones, and so forth.

Mr. **Patman**. This bill would include them, and there would therefore be about 45 billion dollars, including them?

Mr. **Goldsborough**. That would be my estimate.

Mr. **Patman**. And your illustration was, suppose that the retailer's discount was 20 percent, that would be 9 billion dollars issued a year.

Mr. **Goldsborough**. Oh, no; I did not say that 9 billion dollars would be issued a year. I was using it for the purposes of illustration——

Mr. **Patman**. That is right.

Mr. **Goldsborough**. And yesterday I said this, that in my opinion, after the interbank currency began to be used and business thoroughly understood that it would always be available to pump money into retail sales, it would so reestablish confidence that, in my opinion, it would not have to be used except only occasionally.

Mr. **Patman**. Suppose that we put enough in to buy the productive capacity of goods and services, and there is real inflation staring us in the face—we all admit that there is inflation coming if something is not done—but suppose that we want to take about 10 or 15 billion dollars of this interbank currency out of circulation, how would we do it?

Mr. **Goldsborough**. You would not wait until you got that much of an accumulation before you started it.

Mr. **Patman**. Then, we will say a billion dollars. How long will that take to take it out of circulation?

Mr. **Goldsborough**. You could do it in several ways under the bill. There is a special section of the bill which gives the Federal Reserve Board the right to raise bank reserves up to 100 percent if it is necessary to do it.

Mr. Patman. That has already been done, and still something else has to be done.

Mr. Goldsborough. You are anticipating a condition which might arise 20 years from now, and I am not going to anticipate that sort of a situation. If we had a 100-percent system under present conditions the banks would not have anything but their capital, surplus, and undivided profits to loan, about 7 billion dollars, so that it would be years and years before the Federal Reserve System would have to put the banks on a 100-percent basis.

Mr. Patman. But suppose that some unusual situation happens, that there is increased circulation and velocity of the wealth that we have now, and by reason of that and of this interbank currency there is danger of inflation and we have to take a billion dollars of interbank currency out of circulation, how will you do it?

Mr. Goldsborough. I have already said that the Federal Reserve System under this bill could take it out of circulation by increasing the bank reserves.

Mr. Patman. But they have already done it.

Mr. Goldsborough. As I said before, you could anticipate anything which might arise or might no arise 20 years from now, but which certainly could not arise for years.

Mr. Patman. I think that it could arise in a year.

Mr. Goldsborough. If you do, you and I simply do not agree.

Mr. Patman. Suppose that it arises in 10 years, how would you take a billion dollars out of circulation?

Mr. Goldsborough. If it happened in 10 years—is that your question?

Mr. Patman. At any time.

Mr. Goldsborough. No; we want something definite. My answer to that is that I do not have the answer to what will have to be done 10 years from now, which is not material to this inquiry.

Mr. Patman. The question is, and it is very material, Mr. Goldsborough, that you have arranged to get this money in circulation, and it looks good to the consumer, because he will get a 15-percent discount, and to the banker, because he will be paid for handling it, and the interbank currency all comes from the Federal Government. You have provided for its distribution, but I cannot see, and I am anxious to see, and I am seeking light and information, how you are going to take it out of circulation.

Mr. Goldsborough. Of course, if that is the specific question, and the necessity for taking it out of circulation ever arises, the bill makes a specific provision that it shall be taken out by means of the Federal Credit Commission requiring the banks to call in the loans or some part of the loans which are based on the credit that they are allowed to issue, based on this interbank currency. The bill specifically provides for that.

Mr. Patman. I do not understand that that will do it. I have here in my hand some scrip that was issued——

Mr. Goldsborough. Why wouldn't it do it?

Mr. Patman. I want to ask you a question based on this.

Mr. Goldsborough. All right.

Mr. Patman. Here is a dollar bill issued by the county of Cuyahoga, in Ohio. The counties save interest on money by issuing this scrip. It is payable at a certain time, and they paid their county employees half in this and half in regular money. The city of Cleveland did the same thing—issued dollars just like regular money.

Suppose that this interbank currency looks like this, and I am a banker, and I have these two dollars in my possession. They are obligations of the United States Government. They are Government I O U's.

Mr. **Goldsborough**. You say so.

Mr. **Patman**. What is that?

Mr. **Goldsborough**. That is what you say.

Mr. **Patman**. You said that, too.

Mr. **Goldsborough**. No; I did not.

Mr. **Patman**. If you did not say that, we will have to start all over again.

Mr. **Goldsborough**. No; we won't do that at all. We have been discussing this bill this time for 2 days, and we discussed it for over a week in the last session, and everybody in this committee, including yourself, I presume, knows that this interbank currency is not paid to the banks—I said it this morning—it is not paid to the banks unless the banks need the cash in order to avoid a run, or something of that kind, or unless the bank is liquidating.

Mr. **Patman**. Let us say——

Mr. **Goldsborough** (continuing). Therefore it is not an ordinary I O U. You say that, but I do not say that. I never have said that, and nobody on the committee, except yourself, thinks it.

Mr. **Patman**. Whose obligation is it, if it is not the Government's?

Mr. **Goldsborough**. It is the Government's obligation, of course——

Mr. **Patman**. Then we are all right.

Mr. **Goldsborough**. But I have not finished. It is the Government's obligation as interbank currency. It is not the Government's obligation in the ordinary sense of money, and you are fully aware of that fact.

Mr. **Patman**. But it is an I O U?

Mr. **Goldsborough**. That is what you say.

Mr. **Patman**. Don't you think that the Government eventually will have to pay it? Somebody eventually has to pay this, and if the Government is not going to do it, I want you to say now who will pay it. Let us say that the worst comes to the worst, and we must anticipate the worst on practically everything in matters like this. Who will have to eventually pay this money? Is it not a fact that the Government will eventually have to do that? Isn't that a fact?

Mr. **Goldsborough**. It depends altogether on whether the money is needed.

Mr. **Patman**. We will say that it is needed. If it is needed, the Government has to pay it, does it not?

Mr. **Goldsborough**. It would only be needed as money in case the banks need cash. The banks would handle this money that they have with the Federal Credit Commission exactly as they handle their present reserves with the Federal Reserve bank. The banks do not loan money; the banks have not got money to loan. The only thing the banks have is enough cash to pay over the counter. The banks simply use the credit based on the reserves they have with the Federal Reserve bank, and it is bookkeeping money, and nothing else, and it is passed by check. These credits would be handled in exactly the same way. There is no difference whatever.

Mr. **Patman**. But it is somebody's obligation. Somebody has to pay it. Let us say that the money is absolutely needed. Who is going to pay it?

Mr. **Goldsborough**. The difficulty is that I do not see the force of your question except as an attempted catch question, and therefore I cannot answer.

Mr. **Patman**. No; it is very material. You provide how the money can be put out, but not how it can be withdrawn.

Mr. **Goldsborough**. Oh, yes; the bill provides for that, and you are fully aware of it.

Mr. **Patman**. Who will eventually have to pay it, if the worse comes to the worst?

Mr. **Goldsborough**. If all other effectual checks have been used up at some mythical time, in the future, then the bill provides that the Federal Credit Commission can require the banks to call in their loans based upon the credit which they are allowed to issue on this interbank currency. The bill provides for that.

Mr. **Patman**. Would that cancel it? I say that it would not cancel it. Here is $2 of interbank currency. I am a banker. I have loaned you $2, based upon this 100-percent reserve.

Mr. **Goldsborough**. I did not say——

Mr. **Patman** (continuing). And you say that the Federal Credit Commission would call that in—call the loan and cancel this?

Mr. **Goldsborough**. No, I did not; not to cancel it, but to prevent inflation. I did not say anything about canceling it. That was your word.

Mr. **Patman**. I was asking you how you would take it out of circulation.

Mr. **Goldsborough**. I have told you.

Mr. **Patman**. And that was my understanding, that——

Mr. **Goldsborough**. I have told you three or four times.

Mr. **Patman**. Do you have to cancel the loan to take it out of circulation?

Mr. **Ford**. Subsection (h) on page 15 answers that question. It reads:

> (h) In the event of the banks having to face an emergency demand for currency by depositors beyond their ability to meet without dangerous forced liquidation of their quick assets, said banks may apply to the Secretary of the Treasury for permission to convert interbank currency into national currency notes by presenting the former for exchange. Banks which have availed themselves of this privilege under pressure of circumstances shall proceed with the orderly realization of their reserves and the curtailment of their outstanding credits until they are again able to restore the national currency so borrowed and reestablish the circulating credits previously established by the interbank currency notes held by them.

Mr. **Goldsborough**. I presumed that Mr. Patman at least had read the bill and had read that section.

Mr. **Patman**. I had read it.

Mr. **Goldsborough**. What was the purpose of your question if you had read it?

Mr. **Patman**. To find out from the author of the bill if these were not Government obligations.

Mr. **Goldsborough**. In view of the fact that you have not read the bill I will give you some more information about it.

Mr. **Patman**. All right. I am seeking light.

Mr. **Goldsborough**. I am reading from page 13, section (d)——

Mr. **Patman**. Just a moment. If a member of this committee can explain how this will be taken out of circulation without the Government of the United States paying it, I want him to speak up now and tell me, because I do not know. I do not believe any member of the committee does.

Mr. **Goldsborough**. I will try to do something for you.

Mr. **Patman**. All right.

Mr. **Goldsborough**. Subsection (d) reads:

> Interbank currency notes shall be accepted for all forms of Federal taxation payable directly by the banks, and may be used by them as bank reserves, dollar for dollar, but not as a medium for expanding private credit in the form of loans built on fractional reserves.

Subsection (e) reads:

> Upon the findings and advice of the Federal Credit Commission indicating that inflationary conditions are tending to arise, the Secretary of the Treasury is hereby authorized and instructed to recall from the banks such amounts of the interbank currency in their hands as may be necessary to establish and maintain monetary equilibrium.

Subsection (f) reads:

> Upon receipt of said notice the banks shall reduce their outstanding credits so as to increase their surplus reserves sufficiently to permit the return of the proportion of the interbank currency notes held by them to the Treasury without impairing their required legal reserves. In carrying out the provisions of this section the banks shall promote an orderly liquidation and shall not use selective methods which would tend to depreciate any special classes of securities such as those of the Federal, State, and municipal authorities, and the bond and stock markets; except with the concurrence of the Secretary of the Treasury.

Subsection (g)——

Mr. **Patman**. I am familiar with that.

Mr. **Goldsborough**. I know, but it will do you good to hear it.

> Nothing in this Act——

I want you to listen to this, because I want to give you a little information.

> Nothing in this Act shall be construed to prevent the use of open-market operations in Government securities or the readjustments of the discount rate by the Federal Reserve banks in maintaining stable conditions in the money market, and nothing in this Act shall be construed to affect the provisions governing the increase or decrease of the required reserves of banks enacted in the Banking Act of 1935, except that the Board of Governors of the Federal Reserve System shall have the power to increase the required reserves of all national and member banks up to and including 100 per centum.

As far as I know, that answers every question that you have asked.

Mr. **Patman**. Of course, the point that I want to find out, Mr. Goldsborough, you have answered by saying that this is an obligation really of the Government, that you cannot give everybody something, you cannot give these consumers 15-percent discount and then pay all banks for handling it, and pay all charges and give everybody something and do nothing to anybody. You have to do something to somebody in order to do something for somebody. In other words, if you give them money, 15 percent of the purchase price, somebody is liable for that, and I think that you made it plain that the Government is liable for it, that the Government is behind it.

Mr. **Goldsborough.** Mr. Patman, you and I have been talking about this thing of the Government bonds, and we talked together about it, and you have spoken about it a great many times on the floor and throughout the country, and you know perfectly well, I am sure, that if the Government should purchase the Government bonds and issue money to purchase Government bonds, it would have to be a Federal issue.

Mr. **Patman.** Sure.

Mr. **Goldsborough.** What is the difference between that and this interbank currency?

Mr. **Patman.** I think that there is a big difference. I have been studying about that very thing. You give every retailer a blank check book on Uncle Sam, and he can handle it any way he wants to, and if he is not caught, he can get any amount of interbank currency he wants, which is just the same as national currency. I will go with you on paying off the national debt, and we will use the national credit for the benefit of the people. I am in favor of that, not quickly, but gradually, eventually paying off the national debt that way.

Mr. **Goldsborough.** You are in favor of putting it in at the top, and I am in favor of putting it in at the bottom.

Mr. **Patman.** No; it saves money. We are paying nearly a billion dollars in interest on the national debt.

Mr. **Goldsborough.** But, as I said, you are in favor of putting it in at the top and I am in favor of putting it in at the bottom.

Mr. **Patman.** No; I will either be in favor of national dividends, consumers' dividends, anything to distribute purchasing power——

Mr. **Goldsborough.** I admit——

Mr. **Patman** (continuing). But I do not want to give J. P. Morgan the same discount on a $5,000 automobile that you give to a farmer on a truck down in your district. That does not make sense to me.

Mr. **Goldsborough.** That is not intended by you, I realize, and I say frankly that that is not intended by you as a demagogic statement, but if I made it I would be a demagogue, because I know that that is not a rational statement.

Mr. **Patman.** Will the gentleman deny that it would not be done under this bill?

Mr. **Goldsborough.** Mr. Patman, of course, everyone who purchases an automobile at retail, or anything else, would get the benefit of the discount.

Mr. **Patman.** Surely.

Mr. **Goldsborough.** And the retailer would get the benefit of the sale, and the wholesaler would get the benefit of the sale, and the manufacturer would get the benefit of another sale of an automobile, and the man who sold the steel and the tin and what not would get his profit, and that money, that ultimate profit, would go to your farmers and raise the prices of what they sell, and anybody can see that.

Mr. **Patman.** So the submerged one-third would be getting this 15-percent discount, but the two-thirds who do not need it would be getting it just the same.

Mr. **Goldsborough.** Mr. Patman, if that two-thirds, and there is not any two-thirds——

Mr. Patman. We will say 50 percent.

Mr. Goldsborough. No; there is not any 50 percent. There is about 3 percent of the people of this country who hold about 87 percent of the wealth of the country.

Mr. Patman. You take time deposits, you know; you cannot say that 3 percent constitute the only people that would not need it.

Mr. Goldsborough. I think that that is about right.

Mr. Patman. Mr. Goldsborough, this 15-percent discount——

Mr. Goldsborough. I have not finished answering that question. When money goes into circulation by virtue of retail sales, as it goes from the producer to the retailer, from the wholesaler to the manufacturer, and then to the prime producer, under our profit system, it accumulates at the top. Something has to be done to get that money back into circulation. It is not only for the benefit of the ultimate consumer that that should be done, but it is for the benefit of the richest man in this country, because when you can increase and distribute production it is natural that real wealth will be for the benefit of everybody, so that if it is necessary to use the taxing power at the top in order to reduce the interbank currency at any time and cancel it in whole or in part, it is economically sound to do it. Therefore, when J. P. Morgan buys an automobile and gets the benefit of the discount, he is the very man who ultimately, if necessary, would be called upon by taxation to reduce the amount of this interbank currency. So you see it works both ways.

Mr. Patman. Wait just a minute. You say that this interbank currency will be reduced by taxation?

Mr. Goldsborough. I said exactly what I said; not what you said, but what I said.

Mr. Patman. I will ask the reporter to read the statement that you just made.

(The reporter read the statement of Mr. Goldsborough, as above recorded.)

Mr. Patman. In other words, the interbank currency will be retired as taxation?

Mr. Goldsborough. As I said before, I said exactly what I said.

Mr. Patman. Of course, if the bill is passed, this discount will become effective immediately, the 15-percent discount. Anybody who goes into any retail establishment in America will get the benefit of the discount, whether it is 10 cents or $1,000. If a man is paying rent for a suite of rooms at the Willard Hotel at the rate of $15 a day, he will get the benefit of the discount; and suppose——

Mr. Goldsborough. How is that? I do not know what you are saying.

Mr. Patman. I say that if he pays rent to the Willard Hotel at the rate of $15 a day, he gets the 15-percent discount, just the same as the fellow who pays 25 cents for a bed in a flophouse on Pennsylvania Avenue.

Mr. Goldsborough. I make the same observation that I made before about demagogic statements.

Mr. Patman. If that is demagogic, the bill is demagogic, because the bill makes it that way.

Mr. Goldsborough. I will tell you what I think about it, and that is this: Of course, I am a witness, and it is fair for me to answer all questions that are propounded, but it just seems to me that Mr. Patman's system is one which involves his testifying. Now, whether or not the committee wants to prolong this sort of thing, I do not know. Mr. Patman has a perfect right to testify himself, and——

Mr. **Patman.** I have a question, if——

Mr. **Goldsborough.** I am willing to stay here for a week if the committee is interested in this discussion, but the discussion up to this time has not involved the technique of the bill. It has not involved the principle of the bill. It has simply involved some imaginary condition which may arise at some time in the future which might interfere with its operation.

Mr. **Patman.** I submit that out of 3 days, this is the only testimony that goes to the heart of this bill, about the details, as to how it will work, the mechanics of it, and this one question occurs to me about this discount: Suppose that productive capacity is being absorbed by the consumers in America in practically all lines, except, say, automobiles and things like that; would you give a 15-percent discount on everything in order to increase the consuming power on automobiles?

Mr. **Goldsborough.** That is a fair question, and the answer to it, as I understand it, is this—that the consumer will have a right to get the benefit of this discount wherever he wants to get the benefit of it, and as long as he is an ultimate consumer, a natural person, he can use the discount wherever it is to his interest to use it.

Mr. **Patman.** You mean on any article?

Mr. **Goldsborough.** On any article sold at retail.

Mr. **Patman.** All right. Suppose that they put all of these automobile factories to work and they are producing about twice as many automobiles as the people need, and that is about the only thing where there is excess production; would you put the retail discount into operation so as to bring the whole country up to the excess productivity of the automobile plants?

Mr. **Goldsborough.** Mr. Patman, you know that there is nothing in this bill like that.

Mr. **Patman.** That is what I am asking you.

Mr. **Goldsborough.** Of course, that is absurd.

Mr. **Patman.** I thought you said you were going to absorb all the production.

Mr. **Goldsborough.** No; I did not say anything of the kind. That was never said here.

Mr. **Patman.** I misunderstood you.

Mr. **Goldsborough.** What the testimony has been, and what the bill says, is that its purpose is to enable the production of the country to increase to a point where it will be within 15 percent of the demand for consumption goods. Now, if anybody is ass enough to build twice as many automobiles as he can sell, he will just have to bust just like he does now. That is all there is to that.

Mr. **Patman.** You do not think that you will experience any difficulty in these several hundred commodities that appear in the price index in arriving at the standard that you have in your bill?

Mr. **Goldsborough.** I think that anything that has any merit in it is difficult. I think that it would require skill. I think that it would require men who are trained, and I think that they would learn as time goes by, but you are aware of the fact that every responsible organization, such as the Brookings Institution, has made very thorough studies of this discrepancy between our productive power and our consumptive power, and while they are difficulties, they are not insurmountable.

Mr. Patman. Yes; I have read their books on that.

Mr. Goldsborough. They are not insurmountable.

Mr. Patman. And I was in accord with the view that we should fix the price level, but I think that if Mr. Eccles and the Federal Reserve Board would try just half as hard to protect the consumers and the producers of this country as they try to protect the ones who hold Government bonds, we would not have the least trouble. You take Government bonds; when they begin to go up and down, the Federal Reserve Board gets into action, and the Federal Reserve Board does something about it, because they can do something about it, and they have the same power to control the commodity price level today, and they have just as much a mandate to control it today as they have to control the price of Government bonds.

Mr. Goldsborough. Of course, I have no objection to your making that statement, but it would be more apposite when your bill is taken up for consideration. That is not the issue involved here.

Mr. Patman. Very sincerely, Mr. Goldsborough, I have studied this bill and have tried to see your viewpoint, and having followed you on other legislation, and having voted with you, worked with you and got Members of Congress to get interested in your legislation, I felt like there was something to this because you proposed it, and because the chairman of the committee insisted that it be given a full hearing, ahead of everything else, and I said to myself that there must be something to this; but, help me God, I just cannot find any way in the world to retire this currency except through taxation, and the distribution of this money, although it is expended for a good purpose, is, I feel, just topheavy with detail.

Mr. Gifford. Does not section 15 do it?

Mr. Patman. I feel like it is impossible.

Mr. Goldsborough. What was that observation, Mr. Gifford?

Mr. Gifford. On page 14. You have read that carefully. Doesn't that do it?

Mr. Patman. You mean about the Government paying it?

Mr. Gifford. When inflation is on the horizon they just send for that money in the bank and tear it up.

Mr. Patman. Who pays it?

Mr. Gifford. Then they contract their credits. I suppose that the dealers in the communities who got the credits did not demand the actual cash. They kept the credits in the banks and the banks could get the money when they wanted it, but here is a time when they fear inflation, so they order whatever money they had taken returned to Washington.

Mr. Patman. And canceled?

Mr. Gifford. If they cancel it the obligation would be done away with. If you give a check and it goes all around and it comes back and never touches the bank it is a nice proposition.

Mr. Patman. If I felt that we could amend this bill so as to distribute purchasing power, I would stay here days and nights and holidays to try to bring that about.

Mr. Gifford. I must defy you, Mr. Patman or Mr. Goldsborough, to explain this subsection (f), on page 14. That cannot be done.

Mr. **Patman**. I will make this statement, that I do not believe that Mr. Goldsborough can name one Member of the House of Representatives or of the Senate who will vote for a bill like this, and that goes for this committee, too.

Mr. **Goldsborough**. Of course, Mr. Patman, I have not been shopping around for this bill at all.

Mr. **Patman**. The committee has heard the testimony.

Mr. **Goldsborough**. I know that they have, and whether they will vote for it or not, I cannot say, because I have not asked them to and shall never ask them. I am not going around and trying to get promises of people to vote for this bill or anything else.

Mr. **Patman**. I was not suggesting that.

Mr. **Goldsborough**. And they will have an opportunity to vote either for or against it.

Mr. **Patman**. I venture to say that the gentleman himself will want it substantially amended before he will vote for it.

Mr. **Goldsborough**. No.

Mr. **Patman**. Will he vote for it as it is?

Mr. **Goldsborough**. Of course, I prepared it with great care, and it is the best result I have been able to get after 30 years of study of this problem.

Mr. **Patman**. Your objective is fine, and I am with you on your objective, to distribute purchasing power among the masses, but out West the cattlemen learned a long time ago that you cannot fatten the entire herd of cattle by feeding the bull. You have to distribute the feed.

Mr. **Goldsborough**. What has that to do with it?

Mr. **Patman**. It is the same way in this case; you have to distribute purchasing power.

Mr. **Ford**. Mr. Goldsborough, will you permit me to make an observation on (h)?

Mr. **Goldsborough**. Yes; I hope you will.

Mr. **Ford**. There have been a great many questions as to whether or not interbank currency is a Government obligation, and who will pay it in the end. You have provided for the banks converting it into currency, have you not, in (h)?

Mr. **Goldsborough**. Yes.

Mr. **Ford**. You say:

> In the event of the banks having to face an emergency demand for currency by depositors beyond their ability to meet without dangerous forced liquidation of their quick assets, said banks may apply to the Secretary of the Treasury for permission to convert interbank currency into national currency notes by presenting the former for exchange.

That is clear.

> Banks which have availed themselves of this privilege under pressure of circumstances shall proceed with the orderly realization of their reserves and the curtailment of their outstanding credits until they are again able to restore the national currency so borrowed—

Which means back to the Treasury—

> and reestablish the circulating credits previously established by the interbank currency notes held by them.

Now, we will assume that a bank has exchanged interbank currency for a million dollars, and they have a million real dollars that they can pay out to clear up their situation, and finally they get back to normal and the emergency is over. Then what do they do? They have then to repay the Government in regular currency the amount of money that they got from the Government in exchange for the interbank currency, do they not?

Mr. Goldsborough. Yes, sir.

Mr. Ford. Where do they get that money to pay the Government back?

Mr. Goldsborough. From their deposits.

Mr. Ford. They get it out of their profits. They have to have their money there.

Mr. Goldsborough. No; they do not have to have the money, because the Government has given them the money.

Mr. Ford. Well, I would say that under any sane interpretation of that clause, the bank would ultimately have to make good the 15 percent to the Government, and the only way that they would do it would be out of their profits.

Mr. Goldsborough. No; not at all. The Government owes them that money. If the Government wanted the cash, the bank will have the credit on the Government's books, on the books of the Federal Credit Commission, just as it had before. Instead of having the cash, the banks would have the reserves, which they could utilize to loan, and when they loaned a million dollars to somebody, and that somebody redeposited the loan in the bank, as would be done, then they would have the cash and return it to the Government.

Mr. Ford. Then you are putting the Government in that aerial transaction that we utilize in loaning money that we have not got. The Government would be doing the same thing.

Mr. Goldsborough. As I explained yesterday, if you will change your banking system, it would be perfectly all right for the banks to receive the interbank currency in cash, but if we are going to allow the banking system to remain as it is, to do business on a fractional reserve basis just as they always have, and not interfere with the ordinary transactions at all, the only way to do that is to keep this credit from being converted into cash, because if this credit is converted into cash, it becomes a part of the banks' reserves and would cause inflation.

Mr. Ford. I understand that, and to some extent I think probably that is a very good plan, but what I am telling you about is the ultimate time when the bank has to send its interbank currency to the Government and get real money for it.

Mr. Goldsborough. Let me answer that.

Mr. Ford. It never would occur; it could not.

Mr. Goldsborough. I just want to answer that.

In framing legislation, just like in deciding any issue, you have to take into consideration the probabilities. Now, under this system, if it were put into operation, no bank properly managed could fail; it could not fail if it was properly managed and there was no stealing going on and it was reasonably careful about its loans, because just as long as you are using this discount and keeping the production up to within 15 percent of the capacity of the country to consume, your business transactions would be so uniform that there would be no possibility of bank failures. There would be no possibility of runs on banks; and if the runs occurred, this money would be available to take care of the runs, but the runs would not occur.

Now, then, of course, you are going to have dishonesty in banks just like you had before, and you are going to have bad management. If that takes place, and there is a run on your bank, or a liquidation, then, in that occasional instance, the money would be available. We all know that banks never liquidate unless it is a forced liquidation. I never heard of a bank doing a profitable business that ever thought of liquidating. That won't occur. It never has.

Therefore, it would only be occasionally that this money will be needed, and there is no purpose in the bill to deprive the banks of what belongs to them. The only purpose of having this interbank currency is to allow the banks to operate under fractional reserves, just exactly as they always have been doing. If you were to put this interbank currency, instead of using it as reserves, into circulation, then you would immediately have a tremendous inflation, because it would get into the banks' reserves and be used as a basis for issuing credit.

Now, if you change your banking system and put the banks on a 100-percent basis, of course you would put this money right out.

Now, the operation of this bill might ultimately result in the banks going on a 100-percent reserve basis; but if it did, the banks would be just as well off as they are now. They would have just as much money to loan as they have now, or more. The only difference would be that, instead of having reserves to loan, they would have actual money to loan; that is, they would be on a 100-percent basis. I do not mean to say that they would loan all cash.

Mr. **Ford**. There would be more money, but there would be less volume?

Mr. **Goldsborough**. No.

Mr. **Ford**. Yes.

Mr. **Goldsborough**. Why would there?

Mr. **Ford**. Take a bank with a $500,000,000 set-up. If that is the amount of money that they had, one of those big banks can put away reserves up to 10 percent, or 100 percent.

Mr. **Goldsborough**. Let us say 10 percent.

Mr. **Ford**. How much can they loan on that reserve; take a $500,000,000 bank?

Mr. **Goldsborough**. Ten times $500,000,000 would be $5,000,000,000.

Mr. **Ford**. If they were on a 100-percent reserve basis, how much could they loan?

Mr. **Goldsborough**. They only could loan $5,000,000,000.

Mr. **Ford**. That is what I say.

Mr. **Goldsborough**. But suppose that through the years, Mr. Ford, they had accumulated $5,000,000,000 of this interbank currency. They still would have just as much to loan as before. The only difference would be that they would be on a 100-percent basis instead of on a fractional reserve basis, and this is the most rational way of bringing the banks up to a 100-percent reserve ultimately that I have ever been able to figure out, because they would be brought up to a 100-percent reserve basis very gradually. They would always have as much to loan as now, and when they got to a 100-percent reserve basis, their available assets for credit would be just exactly the same as they are now.

Mr. **Ford**. Then would it not be the Government bringing them up to the 100-percent reserve basis?

Mr. **Goldsborough**. Gradually, yes. For instance, if the Government were to go to work now and pay off $40,000,000 in bonds, that money would go into the banks and be available under our present system as a reserve, and so, in order to prevent inflation, if that were done, the reserve requirements would have to be increased in order to avoid inflation. In other words, if the Government were to take a billion dollars tomorrow for the purpose of paying the national debt, it would produce a tremendous inflation unless it were accompanied by a rise in the reserve requirements.

Mr. **Ford**. Suppose that the United States Government said that it was going to pay off these bonds in interbank currency, and gave the banks this currency and said to them that they had to put that in their reserves instead of their regular operations, would that not accomplish the same thing?

Mr. **Goldsborough**. I did not get that.

Mr. **Ford**. Let us say that the Government wanted to pay off its debt, and in order to avoid inflation it paid it off in interbank currency but insisted that the banks use it for straight reserves, but not fractional reserves, would that not accomplish the same thing?

Mr. **Goldsborough**. I presume that it would. I had not thought of that, but a situation like that could be taken care of in future legislation. It seems to me that today the only thing we have to do is to look at two situations, one the emergency situation in which the country undoubtedly is, and we are going around in a circle about it; nobody knows one damn thing about what the result may be of the various pieces of legislation that we are passing from day to day here; I do not know, you do not know, and the President does not know, and businessmen do not know, and the banks do not know, and the consequence is that we are in a terrible situation.

Now, we have thought, and think today, that the price discount at retail would cure the emergency situation in 90 days; there is no doubt about that, and then we have to consider whether or not it is sound permanent legislation. That is the next question. But we do not have to anticipate a condition which might arise 5 or 10 years from now. In other words, I just think it is a mistake, if you have something that is workable under present conditions, to try to defeat it, and I am not accusing you of that, Mr. Ford; do not misunderstand me, because you have been entirely constructive in this discussion. You may not be in favor of it. I do not think you are, but you have been entirely constructive in what you have said.

Mr. **Ford**. I do not know whether I am in favor of it or not.

Mr. **Goldsborough**. Of course, I do not know anything about that. It is none of my business, as a matter of fact.

Mr. **Ford**. Oh, yes, it is.

Mr. **Goldsborough**. Well, I do not so regard it.

As I said, I think that it is a mistake if you have something workable under present conditions to try to defeat it. It must produce the result that you are looking for now. It seems to me that it is time enough, when conditions change, to create new legislation to take care of the new conditions. Many of the questions asked this morning that, to my mind, were at all basic were based on a condition which the operation of this bill might produce years and years from now.

If our minds operated in that way on all of the legislation that we passed, we would not pass any legislation.

That is true, is it not?

Mr. **Ford.** To some extent.

I might make one observation before we close, Mr. Goldsborough, and that is that I have probably given this bill as careful a reading as I know how. I am sure that I am in complete accord with its objectives. There are certain parts of it that do not quite straighten themselves out in my mind, but here is what I believe, that if the method that you have in mind were possible of adoption and were put into law, and the 15-percent discount were put into effect for, let us say, 6 months, I actually do believe that it would take up the slack between production and consumption. Having done that, if part of the producing element in society immediately went crazy and started to produce on a tremendously larger scale, and we only had a 15- or 20-percent discount in operation, it might be possible to accumulate another surplus which it might be almost impossible to pick up, and I mean without the operation of this bill, and supposing that there were three or four industries that were way beyond the consumptive possibilities in their production, there might be that temporary condition; but if this bill operated the way it is intended, and under the objective that you have, the employment situation would be taken care of, and possibly the device that you have originated in the way of interbank currency might be one way of taking up and doing away with the relief expenditures without actually borrowing money in the country to do it; and if this interbank currency would operate as you think it would, and would go into the reserve of the bank and increase them tremendously without making for a vast inflation, which we all think is somewhat dangerous, though I am not as afraid of it as some people are, but if that would occur, it might be possible that through the device of the interbank currency the relief question might be solved, not in helping us to hand out money to individuals but by giving that vast army of willing workers who would love to work if they got an opportunity, a chance to go and produce side by side with their compatriots.

Mr. **Goldsborough.** You are making a much better speech than I am.

The **Chairman.** We will have to adjourn now until 10:30 a. m. tomorrow.

Mr. **Crawford.** Will Mr. Goldsborough be back tomorrow?

The **Chairman.** Yes, sir.

(Thereupon, at 12:20 p. m., an adjournment was taken until Thursday morning, February 3, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, FEBRUARY 3, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The hearing was resumed on H. R. 7188 at 11 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Williams, Mr. Spence, Mr. Farley, Mr. Meeks, Mr. Kopplemann, Mr. Ford, Mr. Brown, Mr. Patman, Mr. Transue, Mr. Luce, and Mr. Crawford.

The Chairman. The committee will come to order.

Mr. Goldsborough, you may proceed.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND—Resumed

Mr. Goldsborough. Mr. Chairman, I find that in the statement I made to this committee last August there is, I think, a right satisfactory explanation of this so-called interbank currency. I want to read one paragraph, and then to discuss it a little more.

To repeat—

> this currency is a limited issue and is designed to circulate throughout the banking system as the backing for the circulating deposits it has given rise to. In this respect it becomes a revolving fund of permanent deposit money for the support of trade. It can only be recalled if or when there appears to be an excess of spendable money over the volume of goods that would cause an unwholesome rise in prices. The Government under advice of the Credit Commission would notify banks that they should reduce their outstanding credits so as to establish surplus reserves sufficient to permit the return of the required quantity of notes to the Treasury. The process would parallel the increase of reserve requirements or the sale of Government bonds in open-market operations to curtail excess credit.

That is the explanation which I made in the formal statement before this committee last July.

Now I, of course, am not an expert on technique at all, but last night I tried to formulate a practical method of applying this discount. Let us assume that this $10,000,000,000 was set up with the Federal Credit Commission, and there was a bank in my town which was a member of the Federal Reserve and which would use this discount. The Federal Credit Commission would set aside on its books, let us say, $100,000, which would be a charge against the Denton National Bank.

Now, then, a retailer goes into the bank and deposits $8,500, and he deposits also a voucher for $1,500 of this retail discount. That retail discount is immediately charged against the $100,000 which has been put to the bank's credit, and which would leave $98,500 still available for its purposes under that bookkeeping arrangement.

We will assume that the time comes when the Federal Credit Commission decides that an inflationary condition exists—that is, that money is going into the market faster than goods are going in, and that there should be a curtailment of this credit money, and the Government notifies all banks that they should curtail their credit 5 percent, and 5 percent in the case of the Denton National Bank amounts to $1,500. So the Denton National Bank would collect from any source it saw fit $1,500 of money which it had loaned, and that money would be returned to the Federal Credit Commission, and as soon as it was returned, this bookkeeping charge would be canceled and the account would then be reestablished at $100,000.

That is one way it could be done. It is purely a matter of bookkeeping technique; and, as I said before, I am not an expert on that, but that is one way it could be done, and I presume that if this bill became a law, an account would be set up for every bank that the Federal Credit Commission did business with.

Now, when the retailer goes to the bank with $850 and a voucher for $150, he gets credit for the full $1,000, and he is out of the picture, but the situation, as far as the bank is concerned, is that the bank has on its books two accounts. As far as the retailer is concerned, he has his deposit of $1,000 on one book, and then the bank has another book which shows a deposit in his favor of $850 and a deposit in favor of the Federal Credit Commission of $150. That would be the necessary additional bookkeeping as between the bank and the Federal Credit Commission.

Mr. Williams. Right in that connection, let me ask you this: Is that $150 that you are talking about, the 15 percent, an asset or a liability of the bank?

Mr. Goldsborough. That is a liability of the bank.

Mr. Williams. A liability?

Mr. Goldsborough. Yes.

Mr. Williams. It is an obligation of the Government to the bank, is it not?

Mr. Goldsborough. No; it is an obligation of the bank to the Government, just like any other deposit. In other words, instead of the deposit being all in favor of the retailer, which would be an obligation of the bank to the retailer, a part of that obligation is in favor of the retailer and a part in favor of the Federal Credit Commission.

Mr. Williams. Then the bank would owe that back to the Government.

Mr. Goldsborough. Yes; the bank would owe that back to the Government as a deposit liability.

Now, of course, as I said a few minutes ago, that liability of the bank to the Government would be canceled if and when it had to be withdrawn from circulation.

Mr. Williams. You would have to take assets out of the bank to cancel that obligation.

Mr. Goldsborough. Well, the bank would be just exactly where it was before it received the deposit, just like any other deposit. There is no difference. It does not make any difference to the bank whether the deposit is made by the retailer or the Government. As far as the bank is concerned, it would have the $1,000 on deposit, but $850 of that deposit would be a liability to the retailer and $150 would be a liability to the Government; that is, insofar as this separate set of books was concerned.

Mr. **Williams.** But, on the other hand, there would be a liability of 100 percent to the retailer?

Mr. **Goldsborough.** Absolutely, between the retailer and the bank.

Mr. **Williams.** I cannot escape the conviction that there is $115 liability for every $100 of actual assets received by the bank.

Mr. **Goldsborough.** No. You see, the Government has contributed to the consumer $150. That contribution has been made.

Mr. **Williams.** At the same time, it is an obligation of the bank to the Government.

Mr. **Goldsborough.** Yes.

Mr. **Williams.** I am thoroughly honest about it; I cannot see why there is not an obligation there, of liability.

Mr. **Goldsborough.** I am sure that you are honest about it.

Mr. **Williams.** I cannot to save my life see how you are going to keep the bank books balanced when you have liabilities in excess of assets.

Mr. **Goldsborough.** You do not have liabilities in excess of assets, because that liability constitutes a reserve which the bank can loan.

Mr. **Williams.** Is a reserve fund a liability or an asset?

Mr. **Goldsborough.** A deposit is a liability on the part of the bank to the Federal Credit Commission, but it represents a reserve which the bank has; in other words, the bank can loan $150 which it could not have loaned except for this deposit which it has from the Government.

Mr. **Williams.** I understand a reserve to be something that is kept in reserve and on deposit, available for use.

Mr. **Goldsborough.** Maybe you would not want to use the word "reserve."

Mr. **Williams.** In general banking terms, I understand that that is the situation.

Mr. **Goldsborough.** Well, the bank's reserves represent deposits, and they represent money which a bank owes to somebody.

Mr. **Williams.** Is cash in the bank an asset or a liability?

Mr. **Goldsborough.** Cash?

Mr. **Williams.** Yes.

Mr. **Goldsborough.** If cash is the capital, the surplus, or the undivided profits of the bank, then it is an asset of the bank; but if the cash is the result of a loan which the bank has made, and which loan has been redeposited in the bank, it is a liability. The bank owes the money, of course.

I will put it in another way. A bank would owe an amount of money equivalent to the cash, and of course the cash would belong to the bank.

The **Chairman.** In the statements that I have seen and know anything about, the bank considers the cash as part of its assets.

Mr. **Goldsborough.** The deposits they call liabilities.

The **Chairman.** They put the cash in one column; on one side they put what they have, beginning with their capital, surplus, undivided profits, and cash; and they put their bonds, or whatever they have with which to discharge their liabilities, in the other column. The cash is part of the assets.

Mr. **Goldsborough.** You may be right about it. It is a bookkeeping process, and I am not a bookkeeper, but that sounds about right to me.

Mr. **Williams.** The reserves would be an asset, would they not?

Mr. **Goldsborough.** I presume that they would get on the asset side of the ledger. I should think so.

Mr. **Williams.** Are you going to use this money as a reserve in the bank?

Mr. **Goldsborough.** Yes, if the 15-percent discount was in operation, $150 of that $1,000 deposit——

Mr. **Williams.** Instead of it being a liability, it becomes an asset?

Mr. **Goldsborough.** It becomes an asset in the sense that the bank has a right to loan $150.

Mr. **Williams.** Well, I do not know of any other item in a bank statement that is considered both an asset and a liability at the same time.

Mr. **Goldsborough.** Of course, as I have said several times, I am not enough of a bookkeeper to work that out for you, but to my mind there is no particular difficulty about it. For instance, suppose that under the old system, before the reserves were raised, the bank had $20,000 in cash, and it was in its reserve. They did not have it in the bank; it was in its reserve. That enabled the bank to loan $200,000; all it had to do was to obtain the 10-percent reserve, and it could loan $200,000.

Now, suppose that in addition to that the bank has $10,000 of this interbank currency. Then the bank could loan $210,000. In other words, this bill is so framed—at least, that is the attempt—so as not to interfere with the ordinary banking processes. It is simply an addition to the present banking process, and a part of that mechanics is that the bank has a right to loan an amount equal to the amount of the interbank currency which it has.

Now, as to the bookkeeping process, that is, as to a suggested bookkeeping process, I have here a suggested plan gotten up by Mr. Harvey, which I had not part in making up and which I have not heretofore seen. He has just completed it and brought it up here, but with your permission I will go over it.

In order to illustrate the way in which the accounts represented by the expansion of credit to consumers would be handled on the books of the banks, a hypothetical set-up is given. Taking first the books of the United States Treasury—Mr. Harvey, will you come up and explain this, please, for me? Bring up a chair. You were kind enough to fix this up, and I would appreciate your explaining it to the committee, because I do not understand what you did.

STATEMENT OF EDWARD F. HARVEY

Mr. **Harvey.** Good morning, Mr. Chairman and gentlemen.

I think that this set-up is already in the record, because it has accompanied one or two of my statements, I think, but I feel very sure that it is in the record.

Mr. **Goldsborough.** But it has not been printed yet.

The **Chairman.** If it has not been incorporated into the record heretofore, it will be put in, but we do not want it in twice.

Mr. **Harvey.** This is the illustration of the bookkeeping of the bank, which would show the obligations between the United States Treasury and the banks—this is throughout the country—in connection with this expansion of credit. It starts with the books of the United States Treasury, and under the formula provided in the bill there is apparent a productive capacity of $30,000,000,000 which is now being unused, which cannot be used under the present financial set-up. On the basis of that $30,000,000,000 of interbank currency notes are authorized under the bill, to be issued to the banks.

I think that the circulation of those notes is understood. The notes would circulate as United States currency within the banking system, but not outside of it. In other words, it would not be an inflation of greenbacks. That is the theory behind it. It is an expansion of the same type of bank credit that the banks now issue, where a customer goes in and borrows money, precisely the same principle of issuing money and circulating it throughout the banking system by check. That is the theory behind these notes, The notes pass from bank to bank simply as the warrants for the credits issued under the bill, and as the money flows from private bank account to private bank account through the check system.

The way that that would be handled in the banks is this. Taking a single bank, which had received, we will say $2,000 face value of retail discount vouchers from 10 retail customers, then the bookkeeping entries of the bank with its 10 retail deposit customers who would have deposited a total of $2,000 in discount vouchers would be as follows—and this is bank A, we will call it:

On the customer's ledger there would appear discount voucher deposits of $2,000, and the customer's ledger would, of course, still have in it the current deposits in the ordinary course of business, so that those current deposits would be increased by the $2,000 arising from the voucher credit.

Mr. **Williams.** There is $2,000 of additional liability created there.

Mr. **Harvey.** There is an additional liability of the bank on the credit account to the customer.

Mr. **Williams.** In other words, you have created $2,000 of liability there on the books of the bank, for which the bank has received nothing so far.

Mr. **Harvey.** The bank, when they make that deposit, will apply to the Treasury for the Treasury notes.

Mr. **Williams.** But so far it has received nothing at all?

Mr. **Harvey.** No; but it will receive——

Mr. **Williams.** All right.

Mr. **Harvey.** But when you say so far it has not, this is the exact point when it gets something. It gets these notes.

Mr. **Williams.** When it gets the notes, it must place them over on the asset side, to balance that additional liability.

Mr. **Harvey.** No.

Mr. **Williams.** How are you going to keep that account balanced?

Mr. **Harvey.** They way it works out is this. The customer's general debit ledger balances with the general deposits ledger in the bank, and the customers' credits arising from discount vouchers balance with the interbank currency notes accounts debits, and the general ledger deposit account debits arising from the receipt of interbank currency notes balance with the interbank currency notes account credits arising from the issue of certificates to bank A.

So that there is a complete balance there.

Mr. **Williams.** A balance by putting the interbank notes in there is an asset?

Mr. **Harvey.** With interbank currency notes as an asset; yes.

Mr. **Williams.** Then you have a voucher with that, put in as an asset?

Mr. **Harvey.** Yes.

Mr. **Williams.** Right there, in that connection: When you withdraw that, when the time comes that that $2,000 is withdrawn, where do you place it?

Mr. **Harvey.** When it is withdrawn?

Mr. **Williams.** Yes.

Mr. **Harvey.** The bill provides for the withdrawal of that by the Treasury under these conditions——

Mr. **Williams.** I understand that, but my question is, What do you put in the place of it to keep your accounts balanced when you pay it out of there?

Mr. **Harvey.** We do not put anything in the place of it. We cancel credits, just as they would be canceled today. They are canceled in exactly the same way as a deposit arising from a note is canceled when the note is paid.

Mr. **Williams.** All right. You call in your credits?

Mr. **Harvey.** Yes.

Mr. **Williams.** That is an asset, is it not?

Mr. **Harvey.** It does not increase the assets of the bank.

Mr. **Williams.** Do you not put your loans, your individual loans, over in the asset column?

Mr. **Harvey.** Yes.

Mr. **Williams.** Of course; and you simply take the money out of that asset. You are taking it out of the assets, are you not?

Mr. **Harvey.** Yes. You are putting on the debit side——

Mr. **Williams.** You call in $2,000, we will say, of notes that the merchants or the farmers owe the bank?

Mr. **Harvey.** Yes.

Mr. **Williams.** Now, that comes out of the already existing assets in the banks. They are assets of the bank, are they not?

Mr. **Harvey.** They are assets offset by equivalent liabilities.

Mr. **Williams.** That is what I am talking about. You say that you call in those credits.

Mr. **Harvey.** Yes, sir.

Mr. **Williams.** And you get the money for them.

Mr. **Harvey.** No. You cancel the money as the result of doing so.

Mr. **Williams.** When you call them in, and the man comes in and pays the money to the bank, that has not increased the assets a cent, has it?

Mr. **Harvey.** No.

Mr. **Williams.** You simply transform the paper assets, the loans, into cash?

Mr. **Harvey.** Yes.

Mr. **Williams.** And your assets are just the same as they were before?

Mr. **Harvey.** Yes.

Mr. Williams. You send that $2,000 in cash to the Treasury, and what is the reason that you are not short $2,000?

Mr. Harvey. You do not send the cash to the Treasury.

Mr. Williams. What do you do with it?

Mr. Harvey. The whole thing is canceled out when a bank calls a loan, and it is paid. They do not send the cash to the Treasury. There is not any cash. That is the point, I think.

Mr. Williams. What do they cancel?

Mr. Harvey. There is not any exchange of money at all in a transaction of that kind.

Mr. Williams. What do they cancel? You say that they cancel it out.

Mr. Harvey. They cancel the circulating deposit which they have issued against a promissory note.

Mr. Williams. Do you mean that they cancel $2,000 of interbank currency?

Mr. Harvey. They might do that if the credit had been issued on the interbank currency.

Mr. Williams. Then you would still be the $2,000 short.

Mr. Harvey. No; because there was not any $2,000 to start with. There was a deposit. That is really the most important point in this whole banking side of it.

Mr. Williams. It is so important that I cannot get it into my thick head.

Mr. Goldsborough. It is very necessary that this be understood, because this is the one thing that is left that is not clear to the committee, and we ought to talk about it until we can get it clear.

Mr. Williams. I believe that we should, and if there is anybody that has the ability to put that into my thick head, I would be glad to have it.

Mr. Harvey. Well, sir, I think that there is one point that must be developed, and that is that the bank money that is represented by credit deposits, by the credit that you have in your bank, is not money. There is nothing behind it. There are 53 billions there in the banks today, and there are 6 billions of United States currency circulating throughout the Nation. That is all of the money that there is.

Mr. Williams. Let me ask you this, and I am talking about it as a purely practical proposition and as balancing the banks' account.

Mr. Harvey. Yes, sir.

Mr. Williams. You know, of course, and everybody knows that the banks' accounts of all assets and liabilities must balance. That is a matter that everybody knows, for if you want to conduct business at all, you cannot have your liabilities greater than your assets and maintain a solvent institution. You have to keep them balanced.

Mr. Harvey. Yes, sir; and it is almost impossible to carry in your mind a balance-sheet operation such as I have in this paper here without having the paper before you. One must look at it and study it on the paper.

Mr. Williams. But I am talking about tangible things. The assets of the bank are real tangible things, are they not?

Mr. Harvey. Not always.

Mr. Williams. Aren't they? What is an asset of the bank that is not?

Mr. Harvey. The assets of the banks?

Mr. **Williams**. Mention one of them; mention an asset of the bank that is not tangible.

Mr. **Harvey**. I should say an asset of a bank which is represented by a single-name promissory note.

Mr. **Williams**. The note is there.

Mr. **Harvey**. It is a promise to pay, that is all.

Mr. **Williams**. All right. It is there. It is an obligation backed up by the moral and financial responsibility of the individual.

Mr. **Kopplemann**. Not moral any longer.

Mr. **Williams**. Well, that might be. But here is a municipal, State, or Government bond, or an industrial bond; those are assets. Here is your cash. Here are your bank building and your equipment, and some other things.

Mr. **Harvey**. They are not very good assets, are they?

The **Chairman**. Talk about the bookkeeping part of it, not the actualities.

Mr. **Williams**. They are actual assets. They may not be 100 percent good; some of them are not, but that is the system that is used in keeping the books, and it is shown in the one column what the bank has, what it owns, what is in its possession. In the other column are its liabilities.

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. Those things are tangible, are they not? They are supposed to represent the tangible wealth of the Nation?

Mr. **Harvey**. Yes.

Mr. **Williams**. Of the individual, the corporation, or the Nation?

Mr. **Harvey**. The balance sheet is the same, whether it is a corporation or a bank or a State.

Mr. **Williams**. That is true. The assets are in there, whether they are individuals, corporations, or the Government, and they represent the obligation of somebody to pay that bank so much money, do they not?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. Those are the assets?

Mr. **Harvey**. Yes.

Mr. **Williams**. And they are tangible?

Mr. **Harvey**. Well, we hope they are; yes.

Mr. **Williams**. You have to keep them balanced?

Mr. **Harvey**. Yes.

Mr. **Williams**. And yet you come along here and give a retailer a 15-percent credit, and you create a liability against the bank of 15 percent of the amount that the retailer deposits?

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. You create that liability, and do not put a thing in the world in there to balance it?

Mr. **Harvey**. Might I ask you this? If the United States takes a million dollars around to a bank and says——

Mr. **Williams**. I am asking you a question, and let us stick for a moment to that question. What is there in the bank to off-set that liability when you take that money out?

Mr. **Harvey**. You put in the interbank currency, just the same as if you put in a greenback, and——

Mr. **Williams**. You come back to the same old thing. That is the obligation of the Government to pay the bank?

Mr. **Harvey**. No; it has already paid it. It paid it in advance.

Mr. **Williams**. All right. That is the money that is put in there. That is an asset.

Mr. **Harvey**. Yes, sir.

Mr. **Williams**. Now, I come back to the question and you get back to the same thing over and over again: When the Government takes out that asset, what do you put in there in place of it, to balance your books?

Mr. **Harvey**. You do not put anything in.

Mr. **Williams**. Then your books are not balanced.

Mr. **Harvey**. Maybe there was no——

Mr. **Williams**. Wait a minute. You say you do not put anything in there. Do you stick to that statement, that you do not put anything in when you take that $2,000 out?

Mr. **Harvey**. I think I do; yes.

Mr. **Williams**. How can you balance your books? They were balanced before. While it was in there, the books were balanced. You take $2,000 out of the assets and put nothing in it; how can they remain balanced?

Mr. **Harvey**. You are drawing it from liabilities, from the deposit which is a bank liability.

Mr. **Williams**. You have just said that you put that in there as an asset, to balance your books.

Mr. **Harvey**. Certainly. The deposit is made as an asset, not to the bank but to the Government.

Mr. **Williams**. Not to the bank? How are you going to keep the assets of the bank equal to the liabilities, unless you have assets in there?

Mr. **Harvey**. In precisely the same way they keep the books if a United States bond was in there, or you put a $10 bill in there. It is exactly the same process.

Mr. **Williams**. Suppose that I take out——

Mr. **Harvey** (continuing). If there are no other assets in the bank, the bank will close up.

Mr. **Williams**. That is exactly what would happen if you do not put money in when you take assets out.

Mr. **Harvey**. Absolutely. You would consider that a United States bond or a United States Treasury note is an asset, if it is deposited.

Mr. **Williams**. That is exactly what I say it is, an asset. It is an asset, and if you remove it and put nothing in place of it. That is a fact, is it not?

Mr. **Harvey**. We put a deposit in, and draw it out again, and then there is nothing left.

Mr. **Ford**. The merchant sells to his customer $1,000 worth of goods. Out of that $1,000 he gets $850 in cash, we will say. He takes that $850 to the bank, and deposits it, together with his certificate of discount, and he gets credit on the bank books of $1,000. Then the bank in turn credits the United States Treasury with $150, which it also deposits in this bookkeeping transaction, making this $850 the equivalent of $1,000 in its deposit holdings.

All right; there is $1,000 there. The bank has contributed, through the Federal Treasury, $150 to make that $1,000, and that goes on and it accumulates until there is $850,000 in cash deposited as a result of sales to customers, and there is $150,000 of interbank currency contributed by the United States Government to make the amount $1,000,000. So far the books balance.

Now, then, in the course of events this entire $1,000,000 is withdrawn by the bank depositors, and the bank pay them $1,000,000.

Mr. HARVEY. Yes.

Mr. FORD. $850,000 of that $1,000,000 came from the cash that the customers deposited, and $150,000 of that was contributed by the United States Government, and we will say that the bank, in order to paoy that $1,000,000, must send to the United States Government $150,000 of its interbank currency and receive for that $150,000 of United States currency which it in turn pays out to its customers.

Now, the situation is just this, if I see it at all: The bank is whole; the depositor is whole; the United States Treasury is out $150,000 in currency. Is that not correct?

Mr. HARVEY. That would be right; yes.

Mr. FORD. Well, where is the Government going to get it?

Mr. HARVEY. Under the bill, it is provided that if a condition of that sort arises, where such a claim as $1,000,000 of United States currency is demanded, which the bank does not have in its reserves, that it may then go to the Treasury and make the exchange of interbank currency for United States currency, and a transaction of that sort would virtually constitute a type of run on the bank. It would have to use extra resources if it could not raise it out of its portfolio to get the cash. In that case it would have to make the currency good to the Treasury. Every bank that gets currency is responsible for making that currency good, and the substitute is a courtesy to the bank, to meet the situation, but only a courtesy to the bank to meet the situation.

Mr. FORD. How does the bank make that $150,000 if it has to pay it back to the Treasury? Does it not come out of the bank's profits? If it returns that money to the Treasury, the bank is out $150,000, and there is no way in God's world that you can figure it out otherwise.

Mr. HARVEY. No, sir; the bank is only out owing to the fact that its position is due to an expanded credit condition.

Mr. FORD. You can use all of the terms about expanded credit and all of the rest of the things that you like. I have a headache on this thing, and I cannot see where that $150,000 is coming from except out of the assets of the bank.

Now, let us take a hypothetical opposite and figure it this way. Let us say that the volume of business that the bank is doing as a result of these customers being able to sell their goods is such that the bank's profits would be sufficient so that they could afford to make that present to the Government. If that would work out, I would say that it was a very desirable situation to put the banks of the country in, but since ulimately it has to come out of somebody, unless the Government makes the bank a gift of that money, the bank has to pay it in the end.

Mr. HARVEY. The whole thing revolves around the method of expanding and contracting credit. It is not a question of dollars. It is not a question of currency. The only time it is a question of currency is when the public demands its bank deposits in United States currency. That is the only time it becomes a question of currency, and that generally means an emergency.

Mr. **Ford**. I have a very simple device—and you may laugh at me—for making all bank assets liquid, through a medium whereby they can be put out at any time it is necessary to get the money, and that is to have some central point where they could be liquidated, and loans would be done away with unless they had loaned more than their assets.

Mr. **Harvey**. Mr. Goldsborough's previous bill contained a provision for that very thing to protect the public.

Mr. **Ford**. I remember one speech that the President made in which he said that he would like to see the money of the United States made asset money, and by asset money he meant the goods and services represented by instrumentalities of the group, that went into the banks, that could be made liquid, and if this would accomplish that, you would solve the banking problem, but there is just one little thing in there that seems to be in the way of making this the solution, and that is that stubborn confusion with regard to the $150,000, as to who is going to pay that in the end.

Mr. **Goldsborough**. Let me see if I can make that clear.

Mr. **Ford**. All right.

Mr. **Goldsborough**. Now, if all of the banks in the country were liquidated, then, of course, the Government would have to put up the $150,000. There is not any question about that. But in the absence of liquidation, that money would simply be out in the form of credits loaned by the banks.

Isn't that the situation, Mr. Harvey?

Mr. **Harvey**. Practically.

Mr. **Ford**. You are giving this general application, whereas at any time an individual bank may be called on to liquidate, we will say, $6,000,000.

Mr. **Goldsborough**. Yes.

Mr. **Ford**. Now, in that particular case, that particular claimant has got to have the money.

Mr. **Goldsborough**. All right.

Mr. **Ford**. And the only thing that he can do is to send the notes back to the Treasury and have them exchanged for regular currency, which it pays out over the counter to satisfy the claims of its depositors.

Mr. **Goldsborough**. That would be done—and I do not know whether Mr. Harvey had any objection to saying so or not, but I have not—that would be done with new Government money.

Mr. **Ford**. Then it resolves itself into what I said earlier in this discussion—that this was merely a subtle device for drawing into the circulating medium of the Nation a sum equivalent to the difference between the money that was available for the purchase of the available production and that production. For instance——

Mr. **Goldsborough**. Yes; but this ought to be added, which is the only thing that makes this bill a vital, living thing, and that is this—that when the new money is put in, it has not been borrowed from a bank; when that new money is put in, every dollar of it is matched with goods that have been sold to the public, so it has not produced inflation. It is not put in at the top, but at the bottom, so that it is all matched with goods.

That is the only thing in this bill that gives it any vitality at all.

Mr. **Ford**. Mr. Goldsborough, I think that I could agree with you if it were not for one point that does not seem to occur to you, and that is this—that you are trying to make it possible to have 15 percent more of the people buy that additional production, and put us in the position where production and consumption are on an equal basis, which is somewhat utopian, but very desirable, and we hope that that can be done; but that would be an ideal situation. But the moment that those goods go into consumption they disappear.

Mr. **Goldsborough**. Yes.

Mr. **Ford**. The system that we operate under at the present time is somewhat similar to it, but the money also disappears, because it only comes in in the form of credit.

Mr. **Goldsborough**. You are right about that.

Mr. **Ford**. So it is still at equilibrium.

Now, if we always knew that for every $10,000 worth of shoes manufactured there is in the system a sufficient amount of money to buy all of the other foods, and automobiles and buggies, and all of the rest of the things that people buy, and, in addition to that, that there is a sufficient amount of currency to take up that additional $10,000, then we would be on an equilibrium as far as production and consumption is concerned; but when that stuff was consumed and the money remains in, and there is a surplus of money, and then, operating your plan as I conceive it to be operated, the necessary concomitant to keeping that in balance would be to withdraw that money, so as to keep the level and avoid so-called inflation.

Isn't that something like you are driving at?

Mr. **Goldsborough**. Could I supplement your statement a little bit? You do not mind my doing it?

Mr. **Ford**. No; I want information.

Mr. **Goldsborough**. I am not any more able to give you information than you are to give it to me, I am sure; but I have attempted to explain what would happen under this bill.

You see, Mr. Ford, if a billion dollars of this money were utilized, and it appeared to the Commission that an inflationary condition existed, or it was about to become very apparent, of course, under the terms of the bill, the money could be withdrawn; but that, in my opinion, is not what would happen at all. This is what would happen: Under the bill, the Federal Reserve Board is given the right to increase the reserve requirements of the banks to 100 percent, and I think as this new money went into circulation the Federal Reserve System would gradually raise the reserves of the banks.

The **Chairman**. Let me ask you a question right there. Suppose that that happened. What would you have gained as a result of your effort to increase the purchasing power by adding this new currency to the already existing volume, for as you raised your reserve requirements, it would have a counteracting effect.

Mr. **Goldsborough**. No; because you put it at the bottom all the time.

The **Chairman**. The raising of the reserve requirements would automatically affect your future transactions, would it not?

Mr. **Goldsborough**. Of course, I have attempted to say and make it as plain as I could that when the time came that the reserve requirements of the banks reached 100 percent, and you could not utilize that device any longer——

The **Chairman.** There would not be any need for it?

Mr. **Goldsborough.** There probably would not be any need for it, but if by reason of this device the confidence of business had not been entirely reestablished, and I think that it would, I do not believe that the device would be needed very often. I do not believe that you would have to use this discount for 6 months before the general public would understand that here was a device which was available at any time, to put money in at the bottom, and I believe that the buying power of the people by virtue of that restored confidence would be so reestablished that you could do away with the device most of the time.

The **Chairman.** But if you did not, a purchaser or consumer who went to buy an article of commerce would continue to avail himself of the benefit of this?

Mr. **Goldsborough.** The bill gives the Commission the right to decide how much discount is needed or whether any is needed.

The **Chairman.** There is one thing about this discussion——

Mr. **Goldsborough.** Before you say that, may I continue a little bit?

The **Chairman.** Certainly.

Mr. **Goldsborough.** I say, if the time should come, and it would be many years in the future, and I do not think that we have to disturb ourselves about it—if the time should come that the reserves were up to 100 percent, then it might be necessary to use the taxing power at the top in order to prevent inflation, but that is a thing that is in the future.

The **Chairman.** What I was about to say a moment ago, and I could not say what the operation would be in detail, is that it does not seem to me that there should be any difficulty in adjusting any situation that would arise by reason of the withdrawal of any of this new kind of currency. In other words, it would be out in physical form in somebody's hands, to be treated as valid within the limitations of law, and that whenever it should be withdrawn or canceled under the operation of the law, there would be no difficulty in adjusting that transaction, so that anybody who happened to hold it would be able in that transaction to treat it as valid, whether it be with the Treasury or with a bank, and if you were to ask me what the mechanics of the bank would be in connection with that operation, I would not be able to say, but I do not understand that it would ever lose its value, or vanish.

Mr. **Goldsborough.** No.

The **Chairman.** So long as it was used within the limits of the law. We will have to quit now.

Mr. **Goldsborough.** Mr. Williams, I have here a copy of that suggested bookkeeping transaction, if you would like to have one.

Mr. **Williams.** I would be glad to have one, but I do not want to be the only one.

Mr. **Goldsborough.** I will have copies made of this other and only other copy that we have.

The **Chairman.** We will meet again tomorrow morning at 10:30.

(Thereupon, at 12 o'clock noon, an adjournment was taken until Friday morning, February 4, 1938, at 10 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

FRIDAY, FEBRUARY 4, 1938

House of Representative,
Committee on Banking and Currency,
Washington, D. C.

Hearings on the above-entitled bill were resumed at 11:02 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present:

Mr. Goldsborough, Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. Evans, Mr. Luce, and Mr. Crawford.

The Chairman. All right, gentlemen.

Mr. Goldsborough, you may proceed.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND—Resumed

Mr. Goldsborough. We were discussing yesterday just what this deposit of interbank currency would represent. I have attempted to get my own explanation in a condition that is satisfactory to myself. To me it is very probable that anything I might say will not be in accordance with bookkeeping practices, but the fact is that I do not know anything about bookkeeping. I am sure, however, that I can make the explanation which was intended by me when I prepared this bill.

We will assume that a bank has furnished this discount and has accepted vouchers from retailers up to the amount of $1,000, which appears on the books of the bank as a deposit by the Federal Credit Commission. Now, ordinarily a deposit represents a debt from the bank to the depositor. That would not be so in this case. The deposit would be owned by the bank in every sense except that the bank could not translate it into cash, so that it would become a part of its reserves upon which it could loan 10 times the amount. It would belong to the bank and be assets of the bank, to take the place of the assets which had been used by the bank and owed to the retailers, except that it could not be used as cash, as a circulating medium, and constitute a reserve, but it would serve the banks in their purposes because it could be used to loan. That $1,000 would be available to the bank to loan to its customers just the same as if it had $1,000 in cash.

Now, the purpose of that, in my mind, is to enable the banks in their usual transactions to continue with their fractional reserves just as they always have done. Insofar as this particular bill is concerned, there is no intention to interfere with the ordinary banking transactions. This is a special service rendered by the banks for which they are paid as provided by the bill, and that service is the transmission of the discount to the consumer. Instead of using this method through the banks, the Government could pass the discount directly to the consumer; but as far as I could tell when the bill was being prepared, that would be an almost impossible way of handling it, and the most convenient way to handle it would be through the banks.

Now, the question arises, of course, if this deposit is really a part of the bank's assets, what right would the Federal Government have to reduce it in amount by requiring the banks to call some of it in? The answer to that is this: If a bank had $1,000 of that sort of Federal deposit, that interbank currency deposit, and one-tenth had to be called in, the Federal Credit Commission would hold that one-tenth for the use of that bank, so that when the time came to expand the bank would get that 10 percent back without having to pay $100 out to any retailer. It would be retained on the books of the Federal Credit Commission as an asset of that bank, to be used later for purposes of expanding the currency, and, of course, would have to be paid to the bank in case of either a voluntary or forced liquidation in cash.

If, as a matter of fact, that process would be considered an unfair process, under the bill the Federal Reserve Board would have the right to raise reserves, which would be exactly the same thing and would put the banks in exactly the same position as if the Federal Credit Commission called in some of this interbank currency. It would not make a particle of difference insofar as the banks' ability to do business and to make money is concerned.

Mr. FORD. And that would put two levers there with which they could work?

Mr. GOLDSBOROUGH. Yes.

Now, Mr. Crawford, I believe that you said you wanted to ask me some questions.

Mr. CRAWFORD. I have several questions that I desire to ask, but I am quite willing to defer to the older members of the committee.

The CHAIRMAN. That is all right. Go right ahead.

Mr. CRAWFORD. Mr. Goldsborough, in view of the fact that this bill, as I comprehend it, deals with the price structure, I have a few questions that I will submit to you.

The other day, while the debate was in Congress on the Navy bill, some Members of the House said that they could not understand why the cost of building battleships had advanced so materially in recent months. Is it not true that our financing and costing system——

Mr. GOLDSBOROUGH. Financing and what?

Mr. CRAWFORD. Financing and costing. Is it not true that our financing and costing system calls for an addition to the selling price of the articles to be marketed, of all costs of every type and character that are incurred or distributed to people in the production of an article? In other words, he who produces and sells must recover all of his distribution made during production in his selling price, or face bankruptcy?

Is that your conception of our financing and costing system, briefly stated?

Mr. **Goldsborough.** That would be so, would it not, in any private system?

Mr. **Crawford.** I think so.

Mr. **Goldsborough.** And it is so with us, of course.

Mr. **Crawford.** Now, in your opinion, is it at all possible for us to find, within the financing and costing system which we follow in this country, an element or elements which will enable a stabilization of incomes or of parity payment, through the lowering of prices, and all to be accomplished through current financial methods? Or will we, in your opinion, be required to go outside the financial and costing system, to some extraneous source such as here presented, for the element of stabilization?

Now, the reason that I put that question that way is that within the last few days we have heard and seen so much in print with reference to the philosophy of Mr. Jackson pertaining to governmental or political control of industry as against Mr. Richberg's philosophy pertaining to his method of control, all having to do with stabilization. Can we find within this financial and costing system under which we operate and which we call a private system——

Mr. **Goldsborough.** As it is at present, you mean?

Mr. **Crawford.** As it is at present—an element which will bring about this stabilization—or do we have to go outside of that set-up to find that element, and does your bill not take one of those elements from the outside?

Mr. **Goldsborough.** Mr. Crawford, I have been endeavoring for many years to find a means of distribution within the present system but have been unable to find it, and I should say that one satisfactory reason for that is that where a labor-saving device is created which takes the place of the units of human labor, the ability to introduce the medium of exchange at the bottom is to that extent lost, because the units of human labor are no longer needed, and the consequence is that the medium of exchange is put into the top, and it simply stays there; so that in a power economy such as we have now I have never been able to find any means whatever of distribution except through a method of reducing the level of the cost of goods to the ultimate consumer at retail.

My investigations have shown me conclusively, from a mathematical standpoint, that that process will not cost anybody anything and will add to the wealth of every class.

Of course, it might be that the additional production which is caused by the operation of such a bill as this might result in some taxation, but the taxation would be only a small percentage of the additional wealth increase which would go to all classes of people—if that answers your question.

Mr. **Crawford.** Let me say it this way: Take the table that is in front of you, and assume that it is the desire of the Government, of Congress, that more tables be produced, distributed, and consumed. Now, the manufacturer of that table has a processing cost in his plant, and he winds up at the end, after having burdened that cost with depreciation, obsolescence, and taxes of all kinds, interest which he pays on borrowed money, and social-security taxes, by the way, and all of the other elements of cost which do not represent purchasing power, which means all those costs other than wages and salaries, and he sums all of that up, and that represents the cost of that product which he is going to pass on to the job, and which cost he has distributed.

Now, he wants to put something else to it which represents a distribution he hopes to make in the future, which we will call his profit or the dividend that he will pay to the stockholders, and he adds that, and let us assume that he passes this table along to the jobber at a cost of $40 per unit. The jobber receives the table at his warehouse, and he adds certain costs which represent cost items other than actual distribution in wages and salaries. Then he adds wages and salaries, and then he adds another item which he calls profit that he hopes to make in the future, which is his profit, and he passes that table along to the retailer at $60 per unit.

The retailer has the table on his floor, and he desires to move it along to the consumer, and, after adding similar costs to those which I have just described, plus a profit, he sells it at $75 to the consumer.

Now, as you move through what, according to my experience and conception, is our present method of operation, you have in that table, at the point of retail, we will say, a mark-up representing profits to be made in the form of future distribution of $15.

We come along and Congress desires that the price of tables shall be reduced, and it is immaterial whether it is tables, shoes, houses, or what not, and we desire to issue an order that retail prices shall be cut in order that the consumers will buy. Those consumers receive wages and salaries out of these different elements of cost which have been mentioned.

Now, the manufacturer, the jobber, and the retailer can reduce their selling price by the amount of profit they have put in there, $15, we will say, but when they do that they cease to make distribution of earnings, which means that they cannot gather back into the building of plants, and jobbing houses, and retail establishments, future capital, because there will be no profit, because of the reduction of the price of the unit to the consumer.

Now, where is there in that whole situation an element which enables this stabilization downward of prices, so that that consumer can buy? Is there such an element in that situation—and I do not want to call it money, because I do not want to get it smeared with the idea of money—that will cause that thing to function as we are attempting to make it function by the laws that we are enacting from time to time, or do you have to go outside of that whole machinery of operation to find an element and bring it in?

Mr. Goldsborough. What we have been doing is to try to perform an impossible task. What we have been doing is to supply the element that you speak of by the creation of debt. That is what we have been trying to do, so that the debts of the country just mount higher and higher and higher, and when they get to a point where somebody gets scared and begins to call in the debt, the whole thing crumbles, and the only way you can start over again is for that debt to be liquidated by bankruptcy and various devices such as repudiation, and so forth.

Now, in order to avoid the necessity of introducing debt as the item which enables the capitalistic process to go on, it is suggested in this bill that society furnish the discount at retail to the ultimate consumer to within 15 percent of the consuming ability of the public.

Now, that is about the situation, as I see it.

Mr. **Ford**. I think Mr. Crawford has forgotten one element in his question. You see, this bill does not contemplate that the manufacturer of tables shall make a discount to the retailer at all.

Mr. **Crawford**. Do not get the record confused on that; I am perfectly clear on that, and I start with the manufacturer, because you have to start with him in order to get to the ultimate consumer, and he is involved in the thing, and there is no way that you can leave him out of the picture.

Mr. **Ford**. He is not involved in this bill.

Mr. **Crawford**. I know that, but I am trying to get at the philosophy back of this bill. We must first find out what we are searching for, and after we find out what we are searching for, then we can dress that thing up to go to the party, but if we do not know what we are searching for; we will not get very far through this committee or any other; and I reemphasize my question. I do not want to go too far with it, because I think other witnesses are going to enlarge on this thing in the hearings on this bill. But is that element in our present system? If not, if we are going to use it, it seems to me that it has to come from some outside source.

Mr. **Goldsborough**. Our present system cannot work permanently, of course. It can only work temporarily, as you inject debt into the industrial process.

Mr. **Crawford**. And that brings you contraction and expansion of credits, with all of the bankruptcies and all of the other things?

Mr. **Goldsborough**. An absolutely necessary accompaniment. You cannot do it any other way.

Mr. **Crawford**. Would this bill, in your opinion, give the public participation in the policy of business, and allow the public to have the degree of protection than bankers find practical for themselves?

Mr. **Goldsborough**. I am not sure that I have the force of your question.

Mr. **Crawford**. I might refer directly to a statement made by Mr. Jackson in New York, I believe last week, where he took the position—and I might say parenthetically that I cannot eliminate the problem discussed in this bill from statements made by Mr. Jackson and Mr. Richberg and all the rest of us with reference to monopolies——

Mr. **Goldsborough**. Mr. Jackson, you must remember, is a lawyer.

Mr. **Crawford**. I understand that, but he is a part of this machine that all of us are mixed up in, and it has something to do with this thing that we are attempting to get at through this bill, and he takes the position that the Government cannot be a party to any kind of a stabilizing scheme having to do with prices and the operation of this business machine unless it in a way protects the consumer's rights and enables the consumer to enjoy a higher standard of living.

So I am back to this question: Would this bill, in your opinion, give the public participation in the policies of business, and allow the public to get less protection than bankers themselves require as they participate in the operation of business, and any good banker will attempt to have some protection, because he has to pay his liabilities in the form of cash through the cashier's window to the men who come in and say, " I want to withdraw my account," so he has to have protection.

Mr. **Goldsborough.** I assume that what you have in mind is something like this, that the banker's point of view, under the present banking set-up, is necessarily the point of view that the more scarcity there is of actual wealth, the more the commodity that he deals in, money, will be worth, and that therefore in order to protect his business, an economy of scarcity is the thing that he instinctively looks for, but the protection that the public wants is not the economy of scarcity which protects the banker, but the economy of plenty.

Now, your question is whether or not, in my opinion, this bill will produce the economy of plenty which protects the public, and my answer is that it is the only thing that I have been able to work out.

Mr. **Crawford.** Have you ever seen anything similar to it in print before?

Mr. **Goldsborough.** Never have, or heard anything.

Mr. **Crawford.** That is the reason why I am interested in getting your views, because you have put more time on this particular thing than any other man I have contacted, and, being a man of years of experience on this committee, I very much respect your opinion, irrespective of what may happen to the bill.

I want to ask you this question, and it is in view of what has been said about the detail involved in the administration of this bill.

We have perhaps 32 million people under the Social Security, and we are carrying a case record on each one, and before they die out we may have another 30 million. That is detail, is it not, the administration and the policing and all of the other things that go with that?

Mr. **Goldsborough.** Yes.

Mr. **Crawford.** Then we have the Federal Deposit Insurance Corporation, over 16,800 banks, and we have the Interstate Commerce Commission, over 85,000 to 95,000 individual truck haulers, and as your railroads disappear you will probably have, with increased production of 80 to 120 billion dollars a year, another 150,000 individual truck operators under the direct supervision and control, with respect to accounting, financing, rates, tariffs, and all that goes with it, of one division of the Interstate Commerce Commission

You have the Securities and Exchange Commission, and we have the agricultural bill that is coming through, that moves in the direction of direct control over six and a half million farmers. We have the Federal Reserve System. We have the State banking supervision.

So, so far as the detailed administration of this bill is concerned, I do not see that it sums up any greater than these others, and I simply throw that in in rebuttal to what has been developed here in this case. Certainly all of these things involve detail.

Now, do you think that the detail involved in the administration of this type of bill is any greater than in these other activities?

Mr. **Goldsborough.** Well, of course, an effort was made to get as nearly absolute simplicity as was possible in order to create a device which would allow the banking system to proceed as it now proceeds without interference, and at the same time introduce into the economic system the very item of which you have been speaking. I cannot see any reason whatever why this bill, if enacted into law, should not operate without any appreciable difficulty after the first few months have transpired. I have said before the committee several times that while I am not an actuary or bookkeeper, I cannot conceive of any greater difficulty in operating the provisions of this bill than in operating payment of a sales tax such as they have in New York. I cannot see it.

Mr. CRAWFORD. You feel that the administration of this bill in its present form——

Mr. GOLDSBOROUGH. Is perfectly feasible; yes.

Mr. CRAWFORD (continuing). Is no more impracticable than the administration of many of these other matters that I have mentioned?

Mr. GOLDSBOROUGH. That is the way I feel.

Mr. CRAWFORD. I wanted to get your statement on that.

Mr. GOLDSBOROUGH. Yes.

Mr. CRAWFORD. Would you mind stating in just as simple language as possible just where or from what sources banks obtain the so-called money for loans?

Mr. GOLDSBOROUGH. Well, as far as the usual methods of banks are concerned, of course, they have some money in the till, which it is necessary for them to use.

Mr. CRAWFORD. I do not mean that kind of money. I mean deposit money created through loans made.

Mr. GOLDSBOROUGH. I know, in case somebody comes in for money, but the real banking business is not transacted with money at all. It is transacted purely and solely by a system of bookkeeping, not involving any money whatsoever except that Congress, insofar as national banks are concerned, has provided that this bookkeeping by which money is created out of nothing shall only proceed in a ratio of around 10 to 1, with what is known as the banks' cash reserves, but as far as any money is concerned, the banks create money out of nothing, and that is generally accepted to be true.

Mr. CRAWFORD. Can you tell us just where it does come from—out of the air, or from public credits, or the national credit, or what do you call the thing?

Mr. GOLDSBOROUGH. It is not anything in the world but the national credit.

Mr. CRAWFORD. I understand the bookkeeping and the philosophy back of it, but what I am trying to get is what that thing is.

Mr. GOLDSBOROUGH. As Will Rogers so aptly said, the banks were the first ones to go on the dole, and the banks, outside of the credit which they get by virtue of the fact that they are supported by the Federal Government, have nothing at all appreciable. It is the Federal credit that gives the banks the ability to do the fractional bookkeeping business that they do do, if that is what you mean.

Mr. CRAWFORD. Would you call it Federal credit or general credit?

Mr. GOLDSBOROUGH. Society's credit. It is the credit of society, of stable government.

Mr. CRAWFORD. That is what I want to know.

With excess reserves on February 2, 1938, being $1,390,000,000, according to the statement that reached my desk this morning, state as simply as you can what amount of manufactured money such as you have just described the banks could issue thereon, provided that the public would accept the issue as money and go along with the banks to the fullest extent permitted under or by law at the present time. What, in your opinion, would be that amount of money?

Mr. **Goldsborough.** How much did you say?

Mr. **Crawford.** $1,390,000,000 of excess reserves.

Mr. **Goldsborough.** It would be about eight times that much.

Mr. **Crawford.** Then this eight times the issue, as you say, would come from the Federal credit or the general credit, or the credit of society, as the case might be?

Mr. **Goldsborough.** That is the only place it can come from.

You used the word "accepted." You said if the public would accept it. The public has not the opportunity to accept it unless the banks are willing to lend it to them.

Mr. **Crawford.** Here is the way I mean to put that question. The law provides that the loan can be made.

Mr. **Goldsborough.** Yes.

Mr. **Crawford.** Suppose that the public, or you as representing the public, should walk up to the counter and say, "Mr. Banker, I desire to make a loan, and here is my collateral," and the banker accepts the collateral, or lends without collateral, then, as you say, if this whole thing functions to perfection, it would mean about 8 to 1.

Mr. **Patman.** Will the gentleman yield for what I believe to be a correction?

Before the reserve requirements were raised, the banks could extend loans at the ratio of about 12 to 1, but since the reserve requirements have been increased 100 percent, it is my understanding that they can now extend loans equal to about 6 to 1.

Mr. **Goldsborough.** You see, a Federal Reserve note is issued on the basis of only 40-percent gold, and the consequence is that when you go into the ramifications of it, you will discover, as I did when I had a talk with Mr. Eccles, one day, when he said that under the 10 percent reserve system it amounted to about 22 to 1, and that would make it 11 to 1 on a 100 percent increased reserve basis.

Mr. **Patman.** There are 2½ dollars for every 1 dollar of gold, and when those 2½ dollars go into the bank, that is a ratio of 6 to 1.

Mr. **Goldsborough.** That is what I am talking about.

Mr. **Patman.** That is on the question of the supply of gold, but he is talking about the excess reserve requirements.

Mr. **Goldsborough.** I have not this morning gone through the process, but I assume that it would be 8 to 1.

Mr. **Crawford.** If the process that we have just described were put into operation, would prices to consumers advance, in your opinion?

Mr. **Goldsborough.** Very much so.

Mr. **Crawford.** Why?

Mr. **Goldsborough.** Well, of course, it would indicate a demand. That demand would have to be created out of borrowed money, but nevertheless it would indicate a demand, and the demand would bring about an increase in prices, so far as I know.

Mr. **Crawford.** I think that that answers it.

Would the credit thus given primarily be advanced to producers, thereby working into this cost plan which I mentioned a while ago, and ultimately resolve itself into the increased price of the unit to be sold to the consumer?

Mr. **Goldsborough.** Yes; these loans will be made to producers, just as you say.

Mr. **Crawford.** And not to consumers?

Mr. **Goldsborough**. That is right.

Mr. **Crawford**. If so, would that not cause an increase in price to the consumer for the full amount of the advance in form of credit granted for production purposes, all of which would be picked up in the cost formula, reflected in increased selling prices to the consumers, thereby nullifying the additional purchasing price created?

Mr. **Goldsborough**. I think that that is scientifically sound; yes.

Mr. **Crawford**. And that is a cycle that we have been traveling down through the years, as you conceive it?

Mr. **Goldsborough**. That is correct, as far as I know.

Mr. **Crawford**. Now, what would be the situation if the credit were granted to the consumer, as in your bill proposed, if I understand it correctly, and thereby kept out of the cost formula?

Mr. **Goldsborough**. Well, the inevitable result would be that the consumption of goods produced would be increased, and speaking in terms of money only for the present, that would mean that the retailer would get more money and more buying power. The jobber would have more buying power. The manufacturer would have more buying power, and the prime producer would have more buying power, and that is the term in which we usually speak, but I thing it is better, if we can do it, to speak in terms of real wealth. I am not so much interested, for instance, in price levels as I am in getting what the country can produce to the people. I think that when that is done, however, it would inevitably result in a practically stable price level.

The thing that I want to do first, and the purpose of the bill first of all is to increase consumption. I feel that the price level would take care of itself.

Mr. **Crawford**. Do you feel, though, based on this last question of mine, that your mechanism issues the credit to the consumer instead of to the producer?

Mr. **Goldsborough**. Yes; that is the purpose of it.

Mr. **Crawford**. And in doing so it keeps the credit expansion, if you call it that, out of the cost formula?

Mr. **Goldsborough**. Yes.

Mr. **Crawford**. And that it does not, in that respect, nullify its objective as the other process does?

Mr. **Goldsborough**. That is correct.

Mr. **Crawford**. That is what I wanted to get at.

Mr. **Goldsborough**. That is stating it better than I have stated it.

Mr. **Crawford**. Do you agree that any policy of inflation, or increase in issues of money or credit in such a manner that it can only reach the public through the medium of costs and be reflected in prices, will inevitably and certainly reduce any financial or economic system to ruin, either temporarily or permanently?

Mr. **Goldsborough**. That is exactly correct, and that is what is happening all the time. I remember very distinctly just a sentence from an editorial in the Evening Baltimore Sun. As you may know, the Baltimore Sun and the Evening Sun are adherents to the present system of finance, very much so, but its sentence was that it was agreed upon by economists that there can be no recovery from a depression until the debts are liquidated which were accumulated during the preceding period of prosperity. In other words, if you have prosperity you have got to have an accumulation of debts under this system, and the greater the prosperity is the greater the debt is, and when the time comes that the creditors begin to fear because of this accumulation of debt, and give demands for payment, the whole thing goes to smash. It is inevitable.

Mr. **Crawford.** In other words, when they begin to call credit?

Mr. **Goldsborough.** When they begin to call credit.

Mr. **Crawford.** Contract credit?

Mr. **Goldsborough.** Yes.

Mr. **Crawford.** Can you tell us how the open-market operations of the Federal Reserve Board would tend to accomplish the result of creating or providing a mechanism to create purchasing power on the part of the consumer and of moving in the direction of trade stimulation, as this bill is supposed to move?

Mr. **Goldsborough.** The answer to that is this, that I think that the open-market operations of the Federal Reserve Board are based entirely on our present conception of the creation of money through debt. When the Federal Reserve System buys Government bonds, and puts cash in the banks which can be used by the banks as their reserves, all that that does is to stimulate the banks to try to loan money. Now, of course, if there is a demand for that money they can loan it, but if the demand does not exist it simply has no effect whatever. As was very well expressed here a few years ago by a witness who said, "You cannot push a string." You can pull a string but you cannot push a string.

Mr. **Crawford.** But if the banks did so loan it would get into production again, would it not?

Mr. **Goldsborough.** If the banks loaned, and the money went into production, and you had a period of bankruptcy and liquidation sufficient to reassure the banks that they could loan, you would have prospered until your debts had accumulated to such an extent as to cause fear and result in another period of bankruptcy.

Mr. **Crawford.** Then do you believe that there is any manner by which the Federal Reserve Board, through open-market operations, can under present laws, attain the objective that you are seeking?

Mr. **Goldsborough.** It is absolutely impossible, in my opinion; mathematically impossible.

Mr. **Crawford.** Do you feel that the bulk of the Federal debt is held mostly by the financiers and financial institutions, or by people who go out and earn wages and salaries and use those salaries and wages in the consumption of goods? Who holds it mostly, in your opinion?

Mr. **Goldsborough.** Someone who knew told me some time ago that about half of the public debt was owned by banks and about half by the public, but whether he meant to include within the public the individual financiers, I am not clear.

Mr. **Crawford.** I am directing my question to those people who draw wages and salaries and have so-called earned income, and use it in the consumption of goods and services.

Mr. **Goldsborough.** My opinion is that half of it is not owned by them.

Mr. **Crawford.** Taking that answer just given, do you know of any way that the purchasing power of the national debt can be reduced without a pro rata reduction of the purchasing power of other descriptions, however small, and all credit instruments held by the general public? In other words, if you reduce the purchasing power of the national debt, or the purchasing power of a $100 bond issued by the Government, is not the purchasing power of all other instrumentalities reduced pro rata?

Mr. **Goldsborough.** Absolutely. It is deflationary, if that is what you mean.

Mr. **Crawford.** Deflationary. Which group, then, of these holders do you think is damaged to the greatest degree when some form of inflation is put into operation, the financier or the man with a great amount of buying power, or the average man whose income is of such a nature that when you reduce its buying power 30 or 40 percent, he tends to move from a comfortable living into or near a starvation realm of life? Who is damaged the worst?

Mr. **Goldsborough.** Of course, the latter.

Mr. **Crawford.** So that ties back to whether or not you will sell goods through retail stores to the consumers?

Mr. **Goldsborough.** That is correct.

Mr. **Crawford.** And that comes directly under the philosophy of this bill?

Mr. **Goldsborough.** Yes, sir.

Mr. **Crawford.** One or two other questions, and I will be through.

Let us get back to the question raised by Mr. Luce the other day, relative to somebody losing $2 on a $10 purchase, that when the woman bought a $10 pair of shoes for $8, the $2 got lost in the shuffle.

The **Chairman.** That should be a dollar and a half.

Mr. **Crawford.** What would be the situation in relation to that question? If someone called you in this morning and said, "Mr. Goldsborough, I have $50,000 in cash, and you have had 20 years' experience. There is a factory across the street, and we can lease that factory. I will put up the money and you put up the experience. We will reach up into the air and bring economic forces together which we know how to operate, and we will start today turning out a certain type of product which, based on our knowledge of improved machinery and momentary technological improvement, and on the condition of the market and the disturbances of labor, we will put a unit on the market at $5 per unit cheaper than it has been sold at any time in previous history," and you start production at the rate of a million units per month and put them on the market, and the article sells for $5 less than the other fellow's price?

Isn't that similar to the type of loss that was referred to by Mr. Luce in connection with this $1.50 transaction?

Mr. **Goldsborough.** There is no loss at all.

Mr. **Crawford.** Isn't that what always happens when you enter the field of declining price levels, where a man actually makes a profit through production instead of a profit through speculation because of an advancing price level?

Mr. **Goldsborough.** That is correct, sir.

Mr. **Crawford.** Are we not perhaps entering into a declining price level over the next 15, 25, or 30 years, or perhaps until another war comes along, and is it not necessary for the operators of American production to put themselves in the position where they will be able to sell in that kind of an economy, instead of on an advancing price level as we have sold in the last 4 or 5 years?

Mr. **Goldsborough.** They cannot distribute under rising price levels to save their lives.

Mr. **Crawford.** If that is the situation that we are up against now, is it not clear that we have to take into consideration, in comprehending legislation along the lines that we now have under consideration relative to monopoly, control, and government-business cooperation, the methods of control indicated in this bill?

Mr. **Goldsborough.** It seems so to me; yes.

Mr. **Crawford.** Do you feel it is possible——

Mr. **Goldborough.** May I interject a statement there which just occurred to me, that I think will clarify a lot of things?

I do not believe that you are ever inflationary when you are increasing the real wealth of a people.

Mr. **Crawford.** By "wealth," you mean goods?

Mr. **Goldsborough.** I mean real wealth, goods. You are inflationary when you put the medium of exchange into the market with no corresponding goods. That is when you are inflationary, and let me go into the matter of the Budget. I do not believe that you can balance the Budget by increasing taxation when it results in decreased consumption. I do not believe that that is balancing the Budget. What I believe is this, that when you are able to distribute to your people all that you can produce in wanted goods, in actual credit, then you will balance the Budget. That is the kind of a Budget we understand, and, reducing that conception to money, which is something which we talk of oftener than we do real wealth, the conception would be something like this: We are now producing 60 billion dollars worth of wealth, real goods. We can produce 100 billion dollars by the operation of legislation such as this. We therefore, by doing that, in the operation of the production of that 40 billions, can reduce our relief load of, I will say, easily 2 billion dollars. That load is taken off of society. Without increasing the ratio of taxation, we can increase our taxes from four and a half billions to six and a half billions, and proceed to pay, then, some 3 or 4 billion dollars a year on our national debt.

So that in this last statement I have made, I have undertaken to show that when you bring consumption and production together, of course it is a balancing of any true budget, and will actually result in balancing your artificial budget which is spoken of in terms of money.

Mr. **Crawford.** Right. Now, if the budget is balanced through an increase in the tax, and that increase in tax, in turn, goes directly back into your cost formula, is reflected in your retail price, would that in itself not defeat this type of bill, even if it be in operation?

Mr. **Goldsborough.** Yes.

Mr. **Crawford.** Because it destroys the ability of the consumer to buy.

Mr. **Goldsborough.** Yes.

Mr. **Crawford.** Do you believe it is possible for technological improvements, based on 150 years of experience, we will say, in this country, to move into this general formula fast enough to always offset—and I am talking about an average over a long period of time—the increase of costs represented by the doubling and trebling of wages and salaries and taxes, and the obsolescence which will follow technological improvements, as well as your depreciation which is also involved in the same case? In other words, can technological improvements be the answer to this thing, or do we come back to the original question, that you have to go outside?

Mr. **Goldsborough.** It cannot, because you cannot build consuming buying power by the creation of capital goods to save your life, but if you give the consumer buying power in the legitimate way, he can create his own capital goods himself.

Mr. **Crawford.** Thank you, Mr. Chairman. That is all I want to ask.

Mr. **Luce.** In the course of your argument, you were speaking of credit and give it no substantial importance. It is a problem that has puzzled me very much, and I would like to get your views about it.

When I go to a bank and borrow $1,000, I pledge myself to turn over to the bank the product of my labor for days or weeks or months to come. Do I understand aright your proposition that that promise to give the product of future labor to somebody else is not a tangible asset, a material asset?

Mr. **Goldsborough.** No. I am not conscious of ever having stated that.

Mr. **Luce.** I thought at one point, in discussing the working of the Federal Reserve System, you went to that extent.

Mr. **Goldsborough.** I did not intend to, sir.

Mr. **Luce.** I may say that what I choose to call artificial capital is one of the important factors in this whole situation.

Mr. **Goldsborough.** I am sorry, but I did not hear that.

Mr. **Luce.** I will repeat it. It strikes me that the credit and debit element ought to get due weight, which I described as the creation of artificial capital.

Mr. **Goldsborough.** Yes.

Mr. **Luce.** One of our common friends, high in the economic world, has denied that in conversation with me. It seems to me that this question of debits and credits in capital ought to be borne in mind.

Mr. **Crawford.** There is another question that I should like to ask, if I may, Mr. Chairman.

Assuming that I should walk up to the bank and say to the banker, "I will offer this collateral; I will even mortgage myself to you for the next 10 years, make a slave of myself," and I thereby secure that loan. Is that not a part of the general credit of American civilization insofar as my individual personality and ability to produce makes it be?

Mr. **Goldsborough.** It seems so, offhand; yes. You see, you are getting into a scientific realm, and you have to be very careful in giving your answers. But it seems so; yes.

Mr. **Crawford.** And if you, the banker, lend me the money, and take my horse or cow, or products, or whether you take my plain promissory note based on integrity, character, ability to work, and physical endurance, it comes back to you again, that general credit, does it not?

Mr. **Goldsborough.** Yes. The thing, Mr. Luce, that I was attempting to demonstrate was this, that under our present system, when debt increases, when you take your note to the bank the first time, it may be said that you have given a fair return for what you have received.

Now, then, as debt increases and prices rise, your assets absolutely rise in value, and therefore you go back to the bank the second time and secure another loan, and each time you go on the increased value of assets due to more of this bank money in operation, and each time you do that, the value of the credit which you give to the bank decreases; it becomes more artificial as time goes by, and eventually the bank gets alarmed and begins to call those notes. When we have that, we have a crash.

The **Chairman**. Some of the Members desire to be on the floor of the House at this time and we will have to recess.

Do you wish to meet again next Monday?

Mr. **Goldsborough**. That is satisfactory to me.

(Thereupon, at 12:02 p. m., an adjournment was taken until Monday morning, February 7, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

MONDAY, FEBRUARY 7, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on the above-styled bill were resumed at 11 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Williams, Mr. Spence, Mr. Ford, Mr. Brown, Mr. McKough, Mr. Barry, Mr. Gifford, Mr. Luce, and Mr. Crawford.

The Chairman. The committee will be in order.

Mr. Goldsborough. Before Professor Spahr begins, I would like to make a statement about a few amendments which it seems should go in the bill in order to perfect it. The purpose of suggesting it for consideration now is to eliminate, if posible, any discussion of matter extraneous to the main purposes of the bill.

Professor Spahr, have you a copy of these suggested amendments?

Mr. Spahr. No; I have not.

Mr. Goldsborough. Then you might want to discuss them.

Gentlemen, it will only take me a minute to make a statement in reference to these amendments. I had a letter from Mr. Ford on Saturday which suggested that paragraph (h) on page 15 should be clarified. It seemed to me that his suggestions were entirely constructive, and an attempt has been made, as you will see, to make an amendment to section (h).

There has been a great deal of very useful and informative discussion as to the preporty rights of the banks in the interbank currency notes, and as to how the books of the banks can be balanced unless the money which they pay to the retailers is returned to them. In that connection an attempt was made in the original bill, which may not have been successful, but which we hope the amendments will make successful, to do this, to give the banks, as individuals, the absolute ownership of the money which they have used for the purpose of compensating the retailers for the discount which they had furnished to the consumers, as individuals, but as bankers the money could only be used for specific purposes, could only be used to be loaned, and could only be converted in case of emergency or of voluntary or involuntary liquidation, and could only partially be used to be loaned once if an inflationary condition seemed to require that all or part of the notes should be called in.

That limitation on the power of the banks, however, only refers to them insofar as the use of the interbank currency notes is concerned within the banking system, but banks, insofar as their ownership is concerned, not insofar as use is concerned, but insofar as ownership is concerned, are compensated by the interbank currency dollar for dollar for the money they expend in furnishing the retailer the funds to compensate him for the discount hat he has allowed the consumer.

We think that the bill as amended certainly does this, and that is all that I want to say.

(The amendments as submitted by Mr. Goldsborough are as follows:)

Page 6, section 6 (a): Omit lines 22, 23, and 24 after the word "order."

Page 13, section 301 (b), line 5: Insert "insofar as possible" after the word "constitute."

Page 14, section 301 (f): Substitute for lines 5, 6, 7, 8, and 9 as far as the period, the following:

"On receipt of said notice each bank holding any amount of Interbank Currency shall reduce its outstanding loans and investments so as to permit the return to the Treasury of its proportion of Interbank Currency notes called in. Such proportion shall correspond to the ratio that the holdings of the said bank bear to the total amount *called* in."

Section 301, page 15, (h): Insert the following at the end of the paragraph in line 15:

"Interbank currency notes exchanged for national currency notes as herein provided shall be returned to the banks when the national currency notes are returned to the Treasury."

Insert here a new paragraph (i) at the end of title 111:

"(i) It is further provided that nothing in this bill shall be interpreted to destroy such ownership as the banks may have acquired in the Interbank Currency notes previously held by them, when or if they are recalled by the Secretary of the Treasury on the advice of the Federal Credit Commission as previously provided. When such notes are so recalled the Secretary of the Treasury shall hold them in trust for the benefit of the banks, until such time as the Federal Credit Commission shall advise that they be returned to the banks which previously held them."

Mr. **Crawford**. Mr. Chairman, before Professor Spahr starts——

The **Chairman**. All right, Dr. Spahr. What are your initials, please?

STATEMENT OF WALTER E. SPAHR, PROFESSOR OF ECONOMICS, NEW YORK UNIVERSITY, AND SECRETARY-TREASURER, ECONOMISTS NATIONAL COMMITTEE ON MONETARY POLICY

Mr. **Spahr** (in answer to the chairman's question). Walter E.

The **Chairman**. This is Dr. Walter E. Spahr, of New York University. You know about him. He is an economist, and he will discuss this bill.

We will be glad to hear you.

Mr. **Crawford**. What are your connections, other than with the university?

Mr. **Spahr**. I am secretary-treasurer of the Economists National Committee on Monetary Policy. I should like to say in that connection, however, that I have come here in my personal capacity. No individual member of that committee may speak for the committee.

Mr. **Gifford**. You came by invitation?

Mr. **Spahr**. I came by invitation; yes.

Mr. **Ford**. We understand that Professor Spahr is speaking purely for himself, do we?

Mr. Goldsborough. I do not know that I extended him an invitation. I extended invitations to a great many people, but the clerk of the committee told me that Dr. Spahr had expressed a desire to come, and, of course, the committee must hear both sides of every question.

Mr. Ford. If I understand it, Dr. Spahr appears in complete opposition to the bill, and therefore we should be glad to hear him.

Mr. Gifford. I do not know that I want to pursue that, but I would like to know his motive in coming here. I have here, for instance, Dr. Spahr's address on the Townsend plan, in which he said that the principles of that plan had gained so much momentum that he felt it necessary to give it some dignified attention.

Is that your reason for appearing here?

Mr. Spahr. No. As secretary of this committee, we try to keep in touch with the bills coming up, and we register ourselves with the House and Senate committees and ask them to notify us if any important bills are coming up for hearing. Then, when one comes up, we notify the chairmen that if it meets with their pleasure we should like to have them invite one or more of our members to come down, and Chairman Steagall kindly extended an invitation to Dr. Kemmerer and myself, but Dr. Kemmerer is away, so we asked Dr. Weyforth, of Johns Hopkins University, to come over, and he is here today.

Mr. Goldsborough. All that I know about it was that Mr. Weed told me that Dr. Spahr would like to be heard, and we are glad to have him, for it would be ridiculous only to hear one side of a question.

The Chairman. I want to suggest that Dr. Spahr be permitted to file his prepared statement with the clerk, and to have it incorporated in the hearing. I assume, Doctor, that you want to speak independently of that, and I suggest that you be permitted to speak without interruption, if you desire to do so, from that point on, when the members will have an opportunity to question you.

Mr. Spahr. I had hoped that I might read my testimony, because everything I care to say is in this statement.

The Chairman. That is perfectly all right, and the members can interrogate you, either then or later.

You may proceed.

Mr. Spahr. This bill is a mixture of the social credit scheme of Major Douglas, the 100-percent paper-money scheme of Prof. Irving Fisher of Yale University, the commodity dollar notion, and the proposal for a Federal monetary authority.

Mr. Goldsborough. What is your authority for saying that Major Douglas and Professor Fisher had anything to do with this legislation, or that they had anything to do with the preparation of the bill?

Mr. Spahr. I would not know that they had anything to do with this bill.

Mr. Goldsborough. You stated that in the same way that you said that I proposed in 1935 a bill which provided for forgery. You are making a false statement about something that you do not know anything about. Professor Fisher and Major Douglas had absolutely nothing to do with the preparation of this bill, and their views are not involved in this bill, as far as I was concerned. They may agree with me—I do not know anything about that—but they had nothing to do with the preparation of this bill.

Mr. Spahr. I did not mean to convey any such thought.

Mr. Goldsborough. That is what you said.

Mr. Spahr. No. I said that the bill is a mixture of the social credit scheme of Major Douglas, the 100-percent paper-money scheme of Prof. Irving Fisher, the commodity dollar notion, and the proposal for a Federal monetary authority. I assume that you are the author of the bill. I knew nothing about the authorship of it.

Mr. Gifford. I want to know Dr. Spahr's definition of "notion."

Mr. Goldsborough. What was your definition of forgery when you accused me of that in the New York Times and the Christian Science Monitor in 1935, and I want to know what was your notion in saying that Lincoln was guilty of forgery when he printed greenbacks in 1861.

Mr. Spahr. I had hoped, if I may say so, that we could stick to the bill.

Mr. Goldsborough. That is what we want to do, and if you will take the material in the bill and go into that I hope that it will help us, but if you are trying to either attack the bill or help the bill by putting somebody else's name to it it will not be of any assistance to us, and that is what you are trying to do, to connect Professor Fisher and Major Douglas with it, and neither one had the slightest thing to do with the preparation of this bill. They are my views, not Professor Fisher's or Major Douglas'. Their views may be more valuable than mine but these are my views, and you won't find on the face of the earth any bill like this by Major Douglas, Professor Fisher, or anybody else in the world.

Mr. Spahr. Representative Goldsborough, I had no thought in mind except to convey as accurate an analysis of this bill as I possibly can, without any reference to any personalities at all.

Mr. Goldsborough. That is what you have done.

Mr. Spahr. No. I merely said that your bill had incorporated in it the notions that you find——

Mr. Goldsborough. I say that it does not provide the notions of anybody else. They are my own notions.

Mr. Spahr. That may be, but they are identical in a good many respect or, perhaps, they have much in common in a good many respects with the social-credit scheme and the other schemes that I have mentioned.

The **Chairman.** Won't you proceed?

Mr. Spahr. Those who have studied the various social-credit schemes, principally that of Major Douglas, are aware of their fallacies, dangers, and failures. The central notion underlying the typical social-credit scheme is that business recessions and hard times are the result of a deficiency in the purchasing power of consumers——

Mr. Ford. What is the reason for a recession except a deficiency of purchasing power?

Mr. Spahr. Are you talking about the present recession?

Mr. Ford. Any recession.

Mr. Spahr. I may say that the best authorities on business cycles would not for a moment say that there is any one cause of any one recession.

Mr. Ford. The real cause is a lack of purchasing power at the moment, whatever the other causes are.

Mr. Spahr. I would not be willing to say that.

Mr. Ford. You may not be willing to say that, but that is the reason.

The Chairman. All right. Go ahead.

Mr. Spahr. The central notion underlying the typical social-credit scheme is that business recessions and hard times are the result of a deficiency in the purchasing power of consumers, and that production and the general level of well-being could be improved if by some device consumer purchasing power could be increased. The usual plan proposed is, in the last analysis, an inflation of the currency.

The fundamental fallacy running through these social-credit schemes is the assumption that consumer purchasing power, in the long run and finally, is not derived from productive activity and may be increased by some juggling device such as the issue of inconvertible paper money.

The Goldsborough bill, H. R. 7188, introduced on May 21, 1937, follows the main essentials of the Douglas scheme and embodies the same fundamental theories, although there are, of course, variations in the details.

Stated briefly, this bill, H. R. 7188, assumes that consumer purchasing power is deficient and can be replenished, not by the economically sound method of increasing production——

Mr. Ford. When the production of automobiles is increased way beyond the power of the people who ordinarily buy them to purchase them, how would you correct that?

Mr. Spahr. I am talking about production in general.

Mr. Ford. Well, they tell us that there is a surplus, that the inventories are way up above what they should be. Why? Because the fellows have not the money to buy.

Mr. Spahr. Inventories are large or small, depending upon the state of the market.

The present inventories probably would not have been very large, or large at all, if the demand could have kept up. That takes us back to the question of what caused the recession, and I say that there have been a multitude of reasons for it. You cannot simplify it and say that one thing, such as the decline of purchasing power, caused it. You have to find out why the purchasing power declined.

Mr. Ford. Can you tell us that?

Mr. Spahr. That is a question not confined strictly to the bill, and my remarks are confined to this bill that is before you.

Mr. Ford. I do not know whether this bill is the solution to our problem or not, but this bill is right on that subject.

Mr. Spahr. Exactly.

This bill assumes that consumer purchasing power is deficient and can be replenished, not by the economically sound method of increasing production but by having retailers give consumers a discount on retail prices. The retailers are to use the vouchers, representing the discounts, as they would acceptable borrowers' paper or cash items, to build their deposits at the banks. The banks are required to create a deposit liability against these vouchers, which are neither acceptable borrowers' paper nor cash items. The banks charge these vouchers to what is called an interbank currency account and then apply to the Secretary of the Treasury for what is called an interbank currency with a face value equal to that of the vouchers. This currency, with certain exceptions pointed out below, is to be used only among the banks as interbank currency and by them in paying Federal taxes. But if bank reserves should be depleted, then these interbank currency notes can be converted into what is called national currency notes, which may be used as money to meet the demands of depositors, thus passing into circulation directly. The nature of the interbank currency and of these national currency notes is not specified, but there is nothing in the bill to indicate that they are not inconvertible and unsecured paper money.

Mr. GOLDSBOROUGH. What you mean by that is that any money issued by the Federal Government and not borrowed from the banks is inconvertible paper money?

Mr. SPAHR. No; I should not say that. I should say that under this plan it would seem that the Government can issue certificates not backed by metallic currency.

Mr. GOLDSBOROUGH. That is your idea, that the Government cannot issue any money except that with metallic currency back of it?

Mr. SPAHR. No. The Government can issue any type of money it pleases.

Mr. GOLDSBOROUGH. But it is guilty of forgery if it does, according to your statement?

Mr. SPAHR. Yes; but do we have to go back to that?

Mr. GOLDSBOROUGH. Is it or is it not? That is what you said a few years ago.

Mr. SPAHR. I should say that it is a defrauding of the people.

The CHAIRMAN. I want to ask you a question on that. Of course, I do not agree with you that the Government has not the right to adopt a method suitable to its own wishes or demands.

Mr. SPAHR. I said that it had.

The CHAIRMAN. As a medium of exchange. The Government has a sovereign right in that matter——

Mr. SPAHR. I agree.

The CHAIRMAN. And it is for the Government to decide what that medium of exchange shall be, and I do not agree with you about that, but, assuming that it should only issue currency against a metal base or metal back, and that is your view of money, is it not?

Mr. SPAHR. So far as Government issues are concerned.

The CHAIRMAN. What other kinds of issues are we talking about except Government issues? That is what I am talking about. That serves as a medium of exchange to transact the people's business.

You believe in a metal base. You would not like to have silver?

Mr. SPAHR. Not any more than is unavoidable.

The CHAIRMAN. And you do not want money based on all of the other resources of the country. Would you be willing for this country now to have a currency backed by a higher percentage than we now have of gold, and cover that entire volume of gold by an issue of currency?

Mr. SPAHR. I see no reason——

The CHAIRMAN. But you are not answering my question. Would you like the Government to do it? You would not want the Government to do that, would you?

Mr. **Spahr.** Yes; I would. I should like to see the Government go back to the gold standard.

The **Chairman.** You are not in favor of the gold standard.

Mr. **Spahr.** Yes, sir; I am.

The **Chairman.** You are in favor of it if it can be manipulated and restricted and commerce crushed and business stifled and suffer distress, so that the people have to be fed by the Government?

Mr. **Spahr.** No.

The **Chairman.** But you are willing today to take gold and put it in circulation, and let business go where it will.

But go ahead.

Mr. **Spahr.** I never have said——

The **Chairman.** You would not dare say that you favor now using our gold as a basis of currency and putting it in circulation?

Mr. **Spahr.** It depends on how you put it in.

The **Chairman.** Go ahead. I got that out of my system, and I don't want to argue too much.

Mr. **Spahr.** You realize that you are putting words in my mouth.

The **Chairman.** The record shows what I said and what you said, and everybody understands the point I am making.

Mr. **Crawford.** May I ask this question?

The **Chairman.** Yes; unless he wants to make a further answer to me. Let him finish answering me, if he wants to. I do not want him to say that I made this record.

Mr. **Spahr.** May I state it briefly?

I advocated a return to the gold standard when the time seems opportune, and that involved issuing gold certificates, if the Government chose to do it. The next important question is the significance of that gold supply in the bank reserves today. The question is whether or not it is wise to continue the policy of sterilization or to dump that imported gold into the Federal banks. That is the important question. That is why it is difficult to give an offhand answer to your question; but I have advocated the return of the gold standard.

The **Chairman.** I do not understand Einstein's theory, but I am talking about your method of putting this money into circulation.

Mr. **Spahr.** I am not advocating putting additional money in circulation.

The **Chairman.** You said that you were in favor of that, provided that you could get it out. I am asking you what that method is.

Mr. **Spahr.** I am not advocating putting additional currency in circulation now.

The **Chairman.** I understand that.

Mr. **Spahr.** But I am opposed to piling up too large a surplus of reserves.

The **Chairman.** What is your method by which you would be willing to issue currency notes, gold?

Mr. **Spahr.** I think that the currency could be issued and a corresponding amount of Government securities retired. Then the Federal Reserve Board would have to watch those reserves to see that they did not become a base for excessive expansion of credit.

The **Chairman.** What you mean is that you would put it in circulation but restrict it so that you could not put it in circulation.

Mr. SPAHR. We raised the reserve requirements under your bill of 1935 to prevent excessive expansion of credit on the basis of reserves, which, I think, was a wise move.

The CHAIRMAN. What would raising those reserve requirements do? What would be the effect of it?

Mr. SPAHR. It probably would not be effective. It might have some effect psychologically. On the other hand, if there should be an expansion, there would exist a large base for a tremendous expansion because of the size of our gold reserves.

The CHAIRMAN. What would the tremendous expansion be?

Mr. SPAHR. It is difficult to say. It depends on the form it takes. It might be an inflation or a sound expansion. If confidence in business should be restored and borrowers began to borrow so that they are utilizing the reserves——

The CHAIRMAN. What you mean is that by raising reserve requirements and restricting credit you would lower prices, or reverse your policy and raise prices and accentuate the circulation of trade?

Mr. SPAHR. No; that is too simple.

The CHAIRMAN. Too what?

Mr. SPAHR. Too simple a statement. Are you referring to the situation in the year 1937, following the rise in the reserve requirements?

The CHAIRMAN. I am not referring to any particular time but making a general inquiry.

Mr. SPAHR. I would imply from your question that you think that by raising those reserve requirements, it precipitated this liquidation. If that is your opinion, I am doubtful about that being the case, because we have large surplus reserves as it is, with reserve ratios where they are. Therefore, to add to those reserve ratios now by dumping that gold back into the Federal Reserve banks might or might not have an effect, since these additional reserves would not be used unless businessmen were to start borrowing. That is a question of general business conditions. If businessmen should start expanding because of a renewed confidence that they might have, perhaps those additional reserves might have some virtue. But these additional reserves could be had later by the reserve banks lowering the reserve ratios.

The CHAIRMAN. What would be the harm in it? Why the fear of adding to your store of reserves and your circulating medium if it will not be effective?

Mr. SPAHR. I think that that is impossible to answer. It is probably a psychological matter, and one cannot gage public psychology very well.

The CHAIRMAN. You would not say that the circulating medium has no basic, substantial, fundamental part in trade and commerce?

Mr. SPAHR. No; I did not mean to convey that thought. I say that my thought there was that you could pile reserves very high, but if the public will not use them, they will lie there.

Mr. GOLDSBOROUGH. What you mean is that you are not in favor of going back to the gold standard?

Mr. SPAHR. No; I would not be afraid of that.

Mr. GOLDSBOROUGH. You want all of this gold to be used as a basis of fractional reserves in the present system, and pile up further reserves? That is what you have to do as you go on the gold standard, as the law now provides.

Mr. **Spahr**. It would be repetition to answer again.

Mr. **Goldsborough**. You need not do it any more, if you are going to say the same thing.

Mr. **Ford**. I move that the gentleman be allowed to proceed.

Mr. **Crawford**. May I ask one question?

The **Chairman**. Yes.

Mr. **Crawford**. If you have answered this, do not say it again, but I am not clear what you mean by convertible and inconvertible unsecured paper money, as set forth in your statement.

Mr. **Spahr**. I used the word "convertible" in the popular sense, that is, silver certificates are convertible into silver, gold certificates are convertible into gold, United States notes are convertible into gold. Of course, the more restricted meaning will be redeemable, as you undoubtedly know. To continue with the prepared testimony:

This currency, with certain exceptions pointed out below, is to be used only among the banks as interbank currency and by them in paying Federal taxes. But if bank reserves should be depleted, then these interbank currency notes can be converted into what is called national currency notes which may be used as money to meet the demands of depositors, thus passing into circulation directly. The nature of the interbank currency and of these national currency notes is not specified, but there is nothing in the bill to indicate that they are not inconvertible and unsecured paper money. The provision for 100 percent of bank reserves opens the way to a 100-percent reserve scheme in which the reserves could be composed of inconvertible and unsecured paper money. The vouchers which give rise to this paper money do not represent the promises of anyone to pay in the future; they are merely pieces of paper indicating the amount of unsecured and inconvertible paper money which it is proposed that the Government shall issue to the banks. It is thus that the provision for currency inflation emerges. The other provisions of the bill throw additional light upon this basic principle underlying the plan.

The chief fallacies of this proposal lie in the assumption that the issue of such paper money, both immediately and in the long run, adds to the real purchasing power of people in general, whereas the fact is that in the course of time the purchasing power of people is reduced. If this were not true, we would not need to concern ourselves about the amount of pieces of paper currency they hold. The assumption that the issue of paper money, rather than an increase in production, can produce more wealth and increase the real purchasing power of people is an economic fallacy.

Mr. **Ford**. Supposing that the United States today, or next year, when the wheat crop comes in, produces the maximum amount of wheat which was produced in 1915, 1,100,000,000 bushels. Do you mean to tell me that that would immediately, and if all other production were on the same basis, produce a purchasing power among the people who want those things?

Mr. **Spahr**. Who wanted to buy the wheat?

Mr. **Ford**. Yes; and the other things that go with it.

Mr. **Spahr**. Oh, no.

Mr. **Ford**. What you are talking about is just plain nonsense.

Mr. **Spahr**. I should not think so.

Mr. **Ford**. Just plain nonsense.

Mr. **Spahr**. You are entitled to your opinion.

Mr. **Barry**. How will they ever get their wheat?

Mr. **Spahr**. From their income from other sources.

Mr. **Ford**. At about 2 cents a bushel?

Mr. **Spahr**. But people that buy wheat are the rest of the populace, and part of the rest of the people——

Mr. **Ford**. The rest of the world is not buying our wheat any more.

Mr. **Spahr**. Whatever their demand is, those people get their income from a multitude of sources.

Mr. **Ford**. I know——

Mr. **Spahr**. Of course you do.

Mr. **Ford**. The rest of the world used to buy about 65 percent of our cotton. They used to buy about 25 percent of our wheat. They used to buy about 25 percent of our corn in the form of hog products, and about the same amount of our manufactures, but they do not do that any more.

Mr. **Spahr**. That is a question of tariffs, partly.

Mr. **Ford**. You admit that that is a question of tariffs?

Mr. **Spahr**. Partly, yes; and a multitude of other things.

Turning from the more fundamental features of the bill to the details involved, other questions emerge that justify scrutiny, comment, and answer. These various significant details will be pointed out in the order that they are mentioned in the bill.

Section 1 declares it—

> to be the policy of Congress to adjust and control the price of commodities sold at retail so as to make it conform to the volume of purchasing power in the hands of the public, and to regulate the purchasing power so that the production of wealth in this country shall be maintained in full measure.

The use of "it" with respect to the prices of commodities is peculiar—the proper word is "prices," not "price."

Perhaps you have corrected that.

What is the meaning of the statement that prices will be made to conform to the volume of purchasing power in the hands of the public? How is this purchasing power measured? And if the purchasing power of people is not sufficient to take goods off the market at asked prices, do not these prices fall? Therefore, do not prices always respond to purchasing power? Is there any purchasing power, in the long run and in the last analysis, except the goods and services offered for sale? Money is merely the convenient medium of exchange, but the final and real purchasing power rests with the goods and services offered for sale.

Mr. **Goldsborough**. Where is that word that you said should be changed?

Mr. **Spahr**. Section I, the word "it." You, of course, mean prices, and not price.

Mr. **Goldsborough**. What page?

Mr. **Spahr**. Your first page, referring to the price of commodities sold at retail. It is in line 7.

Mr. **Goldsborough**. What is your criticism of it?

Mr. **Spahr**. You mean prices and not price of commodities. You are talking about prices of all commodities, I take it, in line 6.

Mr. Goldsborough. Do you mean that you think the grammar is bad?

Mr. Spahr. No; it is a question of individual price, against prices of all commodities.

Mr. Goldsborough. You think it should be "prices"?

Mr. Spahr. You are talking about various commodities, but not one commodity.

Mr. Goldsborough. No; I think "price" is the proper word to use. It is all-inclusive.

Mr. Spahr. Then you mean price level, or price average?

Mr. Goldsborough. No; "price" is the right word. When we get into committee, we will correct that, if necessary, but I think "price" is the proper word.

Mr. Spahr. An increase in the supply of the medium of exchange is one thing; an increase in the supply of real wealth is something else. The two should not be confused as they are in this bill. Surely the world has seen enough instances in which governments have increased the supply of paper money without increasing the supply of real wealth to justify the expectation that confusion of real wealth with pieces of paper money should cease to be a part of people's thinking.

Mr. Goldsborough. Have you read this bill?

Mr. Spahr. Yes.

Mr. Goldsborough. Have you read any of the statements made in connection with the bill?

Mr. Spahr. Only your address in the House.

Mr. Goldsborough. You understand, do you, that the purpose of this legislation is not to let any money come into being until a corresponding amount of new wealth has come into being for distribution?

Mr. Spahr. I am coming to that a little later in my discussion.

Then, what does it mean to say that "the production of wealth shall be maintained in full measure"? There is no one who could know the answer to this question; there are no statistics that could supply the answer; and even if such information were available no person, after careful consideration, would wish to push production to such lengths. This would involve exhaustion of our natural resources now with no regard whatever for the welfare of future generations. In short, section I cannot withstand the simplest sort of economic analysis.

Section II merely announces the social-credit scheme.

Section III (a) mentions the function of interbank currency notes, but does not explain their nature.

(The remainder of Professor Spahr's prepared statement will be found at the end of this day's hearing.)

Mr. Goldsborough. May I interrupt you there? Do you mean to say that we should not supply our people with the things that they need and want in the shape of food, clothing, and shelter because it might interfere with some future generous supply of wanted goods and services? Is that your argument?

Mr. Spahr. No; not at all.

Mr. Goldsborough. My God, then what is it?

Mr. Spahr. I may use your own statement, which is that "the production of wealth shall be maintained in full measure."

Mr. **Goldsborough**. Full measure to the extent of wanted goods and services. Of course, you know that.

Mr. **Spahr**. I do not know what "full measure" means.

Mr. **Ford**. Maybe I can give a definition of that.

Mr. **Goldsborough**. Of course.

Mr. **Ford**. It is as many shoes as the average man will use, as much clothing and food as he can use, and as decent housing arrangement as they can get. Then there are luxuries over and above that, but I am talking about needs now. Wants may be different, such as an automobile, a radio, a fur coat, or something like that.

The **Chairman**. Why shouldn't every family in the country have them?

Mr. **Ford**. There is no reason why they sould not have.

The **Chairman**. Why should some families have them, and others not?

Mr. **Ford**. But I am talking about actual needs.

The **Chairman**. Why should not any man who wants to support his family, if he is an honest citizen, have these blessings, such as a radio, that to me have a spiritual value?

Mr. **Ford**. There are implications in Mr. Goldsborough's bill that he is attempting—and I don't know whether he has the right solution or not; nobody does, but his idea is merely that all goods and services that are produced in this country can only be exchanged by reason of the fact that we have what is known as a medium of exchange, or money. Now, then, if a third, or a half, or a quarter, or whatever part of the population is unable to secure that money, he is attempting, through a device known as the discount, to enable at least 15 percent more of the people who want these things to get them, and he is putting the national credit behind their attempt to do that. That is his philosopohy. Whether it is sound or not, I am not saying yes or no.

But you are arguing that he is merely attempting something that, according to the old theory of economics, is probably fallacious; but according to the old adopted theory of travel, the airplane would be fallacious, as would the automobile and the other forms that we had when we used to travel across the country, at first on foot, later on horseback, then by covered wagon, and then by stage and railroad. Now we have automobiles, trucks, and busses.

Mr. **Spahr**. My point, Mr. Ford, on this specific sentence about the maintenance of the production of wealth in full measure, is that there is no way on earth to measure that sort of thing statistically.

Mr. **Ford**. Will you give us a definition of wealth, right there?

Mr. **Spahr**. The sum total of all values.

Mr. **Ford**. What values?

Mr. **Spahr**. Economic values; everything that has value. If you add it all up, you have our total wealth.

Mr. **Goldsborough**. Do you think that the investigation of the Brookings Institute shows the wealth?

Mr. **Spahr**. No.

Mr. **Goldsborough**. What do you mean? You say that there is no way to reach any conclusion.

Mr. **Spahr**. You are talking about the full measure of wealth. The wealth of people shifts, and their desires and needs shift from year to year, as new products come in. We have no such statistics available, and if you wanted to try this, you could not do it, because we have no statistics to measure any such thing.

That is my point.

The **Chairman**. Would you think it desirable that we should permit at least as full a measure of production as would normally come about from our farms and fields, and factories, without governmental restrictive legislation? Do you think that it would do harm if we had a proper method of distribution, or do you think that we just do not need any better housing, or better methods of transportation, or communication, or social intercourse, and all that?

Mr. **Spahr**. I should answer this way, that we know nothing in economics about raising the standard of living except of increasing the amount of goods for consumption. That is the standard by which we measure the standard of living. That being true, the more goods there are to consume, the higher the standard of living.

Mr. **Ford**. How will you get them?

Mr. **Spahr**. Increased production and better distribution.

Mr. **Ford**. Distribution depends upon the amount of purchasing power in the hands of the population, by and large.

Mr. **Spahr**. In the last analysis, purchasing power comes from production.

Mr. **Barry**. Explain that.

Mr. **Ford**. You are going around in a circle.

Mr. **Spahr**. No; I am not.

Mr. **Barry**. How would you distribute purchasing power, and how will production give them purchasing power?

Mr. **Spahr**. There is no means by which people can get an income except as they produce it, or as the Government hands it out.

Mr. **Ford**. Let us take a concrete example. We have in the United States what is known as the steel industry, and that has dropped from 79 to 43, I think the figures are.

Now, supposing that tomorrow the steel companies and all other companies that are producing went to work and started hell bent for election to produce everything they could. Would that put the purchasing power of those products into the hands of the people that want to buy them?

Mr. **Spahr**. Not necessarily.

Mr. **Ford**. What are you talking about when you say that the standard of living depends on the amount of production?

Mr. **Spahr**. You would put the purchasing power in the hands of employees of the steel industry, to start with, and you know that steel employees do not buy steel, but food.

Mr. **Ford**. They buy automobiles and jackknives and a thousand other things that steel companies produce the raw material of.

Mr. **Spahr**. The point to keep our eyes on is that very few people spend the money for the thing that provides them with their income.

Mr. **Ford**. I understand that thoroughly, but it is an exchange.

Now, here is what I think Mr. Goldsborough's plan would do, and whether he is right on it or not I do not know, but he is trying to pump into the lower level the amount of money necessary to take up the difference between production and consumption, and, using the illustration that was given to us the other day, if there was a 15-percent discount, and the Government stood behind that through interbank currency, these people that would ordinarily buy a pair of shoes for $10 would get those same shoes for $8.50 and would still have a dollar and a half to buy a couple of ties, or maybe half a dozen pairs of socks, and there would be that much more consumption against production, and if that thing went all through the economic fabric of the Nation, the 15 percent would take up the slack and they would start on a new cycle of production, according to his idea. I do not know whether that is correct, and it is opposed to another method, which is to let it all trickle down from the top, like the old story in the Bible of those taking what dropped from the table, and that is about what they have been getting under our system before.

I do not know that this bill is the solution, but I am trying to point out that this silly statement that has been going over the country, and I say that advisedly, that if you will increase production and increase wealth, you will increase purchasing power or the standard of living, is just plain damned nonsense.

Mr. **Spahr**. Then one of the main fundamentals in economics is just nonsense.

Mr. **Ford**. It is nonsense from that standpoint and has been proved to be over the whole cycle of years.

Mr. **Spahr**. I should deny that your statement is accurate.

The **Chairman**. Are you familiar with conditions in the South?

Mr. **Spahr**. Very well.

The **Chairman**. Do you think that the larger the cotton crop down there, the more that our people will have?

Mr. **Spahr**. No. Your point there is overproduction relative to demand in certain lines.

The **Chairman**. Do you think there is an overproduction of cotton?

Mr. **Spahr**. Yes.

The **Chairman**. Have you ever been down South and gone into the homes of the farmers and seen what kind of clothes they have and how much of the consumption of cotton they are permitted to enjoy? They are told, and have been for years, that the reason that they do not have anything is that they produce too much. Do you believe that?

Mr. **Spahr**. Relative to the demand for their product.

The **Chairman**. What do you think is a legitimate definition of "demand"?

Mr. **Spahr**. Demand is simply the amount taken at a given price.

The **Chairman**. That is one definition of "demand." Do you not think that the true definition of demand would be one that recognized, with reference to the distribution of goods and products in this country, the needs and requirements of people living on a standard basis that is at least in a reasonable degree commensurate with the possibility of the distribution of our resources?

Mr. **Spahr**. But that problem is not being met by this bill.

The **Chairman**. I am not asking you that.

Mr. **Spahr**. That is all that I am trying to discuss.

The **Chairman**. You were talking about demand. I am not talking now about the bill.

Mr. **Barry**. You were talking about the people in the South who need the cotton. You mean that if they have $10 with which to buy some cotton, that is a demand for it, even though they may need five or six suits? You mean the purchasing power that they have?

Mr. SPAHR. Exactly.

The CHAIRMAN. That is, their ability to buy.

Mr. SPAHR. Correct.

Mr. BARRY. It is not their demand, but ability to buy.

Mr. SPAHR. That is the definition of demand.

Mr. MCKEOUGH. Do you believe that they would have a larger income if they could increase the demand?

Mr. SPAHR. Certainly.

Mr. MCKEOUGH. Are you in favor of the principle of the wages-and-hours measure?

Mr. SPAHR. That question is so framed that it is difficult for me to answer it, but I should like to answer it this way, that if by regulating all wages and hours you fix a rate which is above a competitive rate, you will increase unemployment, and that the problem is not that of wage rates so much as it is a question of unemployment.

Mr. MCKEOUGH. Production itself, in an academic discussion, does not produce employment, except for the ability of those for whom the production has been developed to buy. If Mr. Ford were to produce 100,000 automobiles, and there were no demand for them, he would not sell 100,000 automobiles. That is obvious.

Mr. SPAHR. Quite true.

Mr. MCKEOUGH. What is the cause of the inability of those that Mr. Ford looks forward to as a potential market for his production to meet his anticipated production scheme? It is a combination of circumstances that prohibits the potential buyer from buying what he produces, because, generally speaking, the buyer does not have enough. Now, if that is the situation, it would seem to me that the requirement primarily before the country is to serve the unemployment situation by making such moves with Government credit as will stimulate the ability of the masses to buy.

Mr. SPAHR. How are you going to do that?

Mr. MCKEOUGH. You certainly are not going to do it on the basis that I have gathered in what I have listened to of your remarks, that is, purely on the basis of going out and producing something.

Mr. SPAHR. When you say that Mr. Ford cannot sell because there is no demand, you have not gone back far enough. Why isn't there the demand?

Mr. MCKEOUGH. Because they have not the money to buy.

Mr. SPAHR. Why?

Mr. MCKEOUGH. Because they have not been able to earn it.

Mr. SPAHR. Now you are getting back to the point. Why have they not been able to earn it?

Mr. MCKEOUGH. Because of a lack of opportunity to get employment.

Mr. SPAHR. Exactly.

Mr. MCKEOUGH. What is your answer?

Mr. SPAHR. My answer to that is this, that producers have hesitated to go forward for a multitude of reasons, and you are acquainted with them, I imagine. Therefore we have had heavy unemployment and consequently purchasing power has lagged. But it serves no useful purpose to talk about the lack of purchasing power. The question is, Why the lack of purchasing power? Purchasing power comes from production. You cannot dodge that.

Mr. McKeough. I think that you are safe behind that smoke screen.

Mr. Spahr. That is no smoke screen.

Mr. McKeough. I think it is.

Mr. Spahr. Where do you get your purchasing power?

Mr. McKeough. From my ability to buy, based on my salary and other means.

Mr. Spahr. That is not where you get your purchasing power. That is spending your purchasing power. Where do you get your purchasing power?

Mr. McKeough. I surely could not buy anything I wanted if I did not have the money to pay for it.

Mr. Spahr. But where do you get your purchasing power?

Mr. McKeough. From my income.

Mr. Spahr. Where do you get your income?

Mr. McKeough. Let us assume that I get it from my salary.

Mr. Spahr. Now, as to the people who pay you, where do they get it? Where does the Government get it?

Mr. McKeough. From the taxes.

Mr. Spahr. Exactly; and where do the people get their incomes to pay the taxes?

Mr. McKeough. From their employment and profit.

Mr. Spahr. And production.

Mr. McKeough. Yes, but you have the cart before the horse.

Mr. Spahr. No, not at all. That is the basic starting point. Power to consume comes in——

Mr. McKeough. Power to consume is different from power to produce. You have two situations. One is production, and the other is consumption.

Mr. Spahr. Exactly.

Mr. McKeough. Your production is dependent on your consumptive power.

Mr. Spahr. You have your cart before your horse.

Mr. Ford. In 1929 the United States produced more goods and services than at any other period in history, did it not?

Mr. Spahr. I am not certain.

Mr. Ford. We will say 1928; 1928 was the maximum. Then why didn't we go on and on and on? What happened then?

Mr. Spahr. Well, we had an international situation, for example, to deal with, which caused the drop in foreign trade. We had a great overreaching of ourselves in speculation. We had an almost endless number of maladjustments following the World War that were operating.

Mr. Ford. But we were producing more at that time? That was our maximum production?

Mr. Spahr. Yes.

Mr. Ford. Therefore we should have continued to have our maximum high standard of living.

Mr. Spahr. A lot of producers overreached themselves did they not?

Mr. Ford. But if production is the thing that governs——

Mr. Spahr. Remember, we do not talk about production except with respect to profits, do we? What I say is that in 1928 and 1929, a lot of men overproduced, they found that further production was no longer profitable, and they had to shut down. That threw people out of employment and reduced incomes.

Mr. **Ford**. Let us keep on the point. You have laid and predicated your whole argument on the basis that the high standard of living is based on high production. That period was the highest productive period in the history of the United States, and still it flopped, because they overreached themselves.

You talk about simplification. You are talking about something that is the ne plus ultra of simplification, that if we just wanted to produce and produce, that would answer all of our problems. Suppose that the steel corporations, General Motors, Ford, Chrysler, and all the rest of them start on a hell-bent program of production; would that solve our problem?

Mr. **Spahr**. You missed the point that I made, Mr. Ford. I said that people do not think of production except with respect to profits. Producers will not produce very long without profits.

Mr. **McKeough**. So production is not the answer, unless the profit is there?

Mr. **Spahr**. People do not produce long without profit.

Mr. **McKeough**. Then that is not the answer?

Mr. **Spahr**. No, sir.

Mr. **Barry**. There are 10,000,000 people out of work, either totally unemployed or employed by relief agencies, according to the census taken last November. Now, what will start the wheels of industry going, when people have no purchasing power?

Mr. **Spahr**. When anything stops production because producers are afraid they will lose profits, they have to work off of their inventories and reduce their costs, so that they can see an opportunity for profit, or some unexpected circumstance must change the demand for their product, or some encouraging circumstance must arise.

Mr. **Barry**. Do you mean that unless we have a war right now, or some other unexpected development, things with these 10,000,000 people will remain in statu quo?

Mr. **Spahr**. Until they work off their inventories.

Mr. **Barry**. How will that help the people? If they work down their inventories, it will reduce production and the people will have no purchasing power.

Mr. **Spahr**. Frequently you get into conditions where you cannot improve rapidly, until you work off your inventories.

Mr. **Barry**. Where will that lead us to?

Mr. **Spahr**. A recession.

Mr. **Barry**. What will that lead us to?

Mr. **Ford**. Let me say this: Did you ever study the situation that developed in 1857?

Mr. **Spahr**. Yes.

Mr. **Ford**. I assume that you did. You are a university man, a scholar and all that. By any chance, do you recall the statement made by—I do not remember the name—a very eminent man at that time, that in 1857 the United States was at the peak of its productive power; we had a great cotton crop; we had a magnificent wheat crop, not as big as now, but big at that time, and we had a tremendous amount of timber, and we were getting into coal then, and some of our ships were taking coal to Europe, and we were on the top of the world; and at the peak of our production, what happened? Do you know what happened in 1857? We had a terrible just plain panic, wasn't it? You recall that. That was a classical example of production gone to its ultimate possibility in a nation, a new nation, and what happened? These people had produced, and done their best and given everything they had, and what happened to them? We were exporting a lot at that time and we were paying our debts. We had borrowed from England and Germany and the Dutch, to develop our mines and our mills, and there was a big foreign debt, and we produced all of this stuff, and the idea was that we were going to ship it abroad, to pay our debts, and all of a sudden that went to nothing. Why? Did you ever look at that situation?

Mr. **Spahr**. I have, and overexpansion of public improvements in this country piled up the debts for public improvements beyond the ability of the population to absorb them.

Mr. **Ford**. But we were at the top of our ability to produce. With that production, the people should have been able to take care of all of those debts, and everything, if production is the root of all this.

Mr. **Spahr**. I think that your statement is far too simple.

Mr. **Ford**. You have said that production is your answer.

Mr. **Spahr**. But you keep forgetting the statement that I made, that production is not made for very long unless there is a profit being made by the producer.

Mr. **Ford**. At that period there were profits being made. A man went out into the woods and cut a million feet of timber, and logged it down to the seacoast and sent it to Europe, and he got a profit out of it, naturally.

Mr. **McKeough**. May I interpose?

If that is the answer, Doctor, the reports that are coming out on the operations of industry in this country for 1937 show that they had a pretty fair year from a profit standpoint, do they not?

Mr. **Spahr**. I think so.

Mr. **McKeough**. What stopped production, then?

Mr. **Spahr**. Loss of confidence, I should say, by businessmen. They did not think that business would continue to be profitable.

Mr. **McKeough**. Then it was not production with a profit that was the answer to the present set-back.

Mr. **Spahr**. That brings you back to the point I have been emphasizing, and that is that when producers are not making profits they will stop producing. That is ordinary common sense.

Mr. **McKeough**. What, in your judgment, was the primary factor for this lack of confidence on the part of businessmen that you have referred to?

Mr. **Spahr**. I should say that there are a good many factors.

Mr. **McKeough**. What is the major one, in your judgment?

Mr. **Spahr**. I think there was talk of inflation that caused businessmen to bid up prices. Then there was the labor movement. Because the labor movement meant driving up wages and costs businessmen piled up inventories in anticipation of strikes and labor troubles—they overstocked. Then there was the unhappy situation in Europe, which certainly had its repercussions. Then there were the taxes of various sorts that disconcerted businessmen. The general discussions in various places regarding credit also disconcerted them, so they lost confidence.

Mr. **McKeough.** Was there any feature of monopolistic price control that may have entered into it?

Mr. **Spahr.** I should think so.

Mr. **McKeough.** Was that a minor or a major factor, in your judgment?

Mr. **Spahr.** I should say it was a factor, but how important it was I should not be able to say.

Mr. **McKeough.** Was it as important as any of the other factors that you have enumerated?

Mr. **Spahr.** I would not have any way to measure how important it was.

Mr. **McKeough.** Would that, in your judgment, have any relation to a continued program of high production?

Mr. **Spahr.** I should say that a monopolistic price that is maintained artificially high would tend to aggravate a situation such as the one we are now in.

Mr. **McKeough.** What is your answer to the strange phenomenon that developed in connection with the heavy purchases by the Government in connection with the naval program, where all of the bidding companies offering bids on armor plate bid the same price?

Mr. **Spahr.** I know nothing about that beyond what I saw in the papers.

Mr. **McKeough.** You read that?

Mr. **Spahr.** Yes.

Mr. **McKeough.** Were you suspicious that there may have been a concerted effort there?

Mr. **Spahr.** It would look that way to me, but I know nothing beyond what I have seen in the papers.

Mr. **McKeough.** Do you think that might have some bearing on the continuing progress of the maintenance of production for the needs of the Nation, from a profit standpoint?

Mr. **Spahr.** I should say that the rigid, artificial maintenance of prices has the effect of aggravating either an expansion or a contraction.

Mr. **McKeough.** Then you would share the point of view of some who are in the school of thought that that has not helped the situation?

Mr. **Spahr.** I would share that view; yes.

Mr. **Gifford.** Tell him what the answer is.

Mr. **McKeough.** I wish I knew.

Mr. **Gifford.** He successfully dodged what you wanted him to say.

Mr. **Spahr.** I know nothing except what I have seen in the newspaper reports. I am not competent to say——

Mr. **Gifford.** You successfully parried his interrogations.

Mr. **Spahr.** I did not mean to.

Mr. **Gifford.** You said that interference and threats have brought upon business a fear that has caused production to curtail.

Mr. **Spahr.** I should say so.

Mr. **McKeough.** Just a moment. May I interpose?

Mr. **Gifford.** Did you not have that in your mind, and the operation of the Walsh-Healey bill?

Mr. **McKeough**. Not at all, and I think that I can answer that by saying this, that prior to any Walsh-Healey bill, the Pennsylvania Railroad started to meet its requirements for the ensuing year, and I understand that they would get the same bid from all of the steel companies.

Mr. **Gifford**. It is not monopoly, but it is cooperative and it is all right when the farmers do it, but all wrong when others do it. Does it not simmer down to this, that when we have a normal production, we have a normal wage and normal purchasing power?

Mr. **Spahr**. I should think so.

Mr. **Gifford**. People who have saved, and those who have been left money, have purchasing power?

Mr. **Spahr**. Yes.

Mr. **Gifford**. What we want to find out is how long we can continue to pump money to these sharecroppers who have been put out of a job. If they have not $10 to buy a pair of shoes, what will we do with them, or with the other unfortunate people?

Mr. **Spahr**. I could not give you an answer to that in simple terms that would be sufficient. These things are too complex to warrant suggestion of a simple solution.

Mr. **Gifford**. Should not the Government print some money and send it out directly, instead of doing all this?

Mr. **Spahr**. That would be the logical thing to do, if you are going to do a thing of this sort, just send a truck down there and distribute the money.

Mr. **Gifford**. And the Government is the ultimate payer of this bill?

Mr. **Spahr**. Exactly.

Mr. **Luce**. Unfortunately, I was not able to hear the early part of your statement, because of attendance in another meeting, and I do not know whether you have dealt with the point that those who produce must sell to those who can buy, and if for some strange and unknown reason a wave of psychology sweeps through the country, those who have money stop spending it.

Mr. **Spahr**. That is true.

Mr. **Luce**. And that has the effect of causing me to wear my old pair of shoes another year, rather than of inducing me to buy a new pair of shoes, and is it not true that in every depression, fear on the part of the consumer is the chief cause?

Mr. **Spahr**. It might be. It often is.

Mr. **Luce**. Do you think that any legislation can cause the buyers who have money to expend next year more than they spent this year?

Mr. **Spahr**. Not unless that legislation restores confidence in some manner, so that they feel that their jobs are going to be intact or improved, their income increased, and confidence restored. Then they might feel justified in spending it. Much of the lack of spending today rests not upon lack of purchasing power, but, as you say, upon fear of the people to spend. They are waiting, keeping their incomes against the day of great uncertainty.

Mr. **Luce**. Mr. Ford called your attention to the prices in 1857. In his first inaugural address President Buchanan set forth the terrible plight of the country, as he saw it, in words just as extreme as those that are used today, and in his next annual message, if I remember it correctly, he pointed out that the country was again prosperous. It took only 12 months to bring about that change. Can you give any reason why, in the present instance, public willingness to buy has not returned?

Mr. **Spahr.** I should not give a single reason. I should give several. Most of them would come under the heading of loss of confidence, fear, costs increased ahead of demand for their products, taxes of a certain type—those are just a few of the reasons that would enter into it, and then there is the international situation, too.

Mr. **Luce.** I have in my pocket now about $20. If the Government put in $20 more, would that increase my willingness to buy, if fear still continues?

Mr. **Spahr.** If the Government printed fiat money and put $20 in every man's pocket, I should suspect that it would destroy confidence in the currency and the people would buy—they would exchange their currency for commodities. In other words, that would be just wild inflation.

There are two types of spending. There is one based upon confidence. There is one based upon fear of the currency.

Mr. **Luce.** We are confronted by numerous proposals of one sort or another to put more money into the pockets of the people, upon the theory that if we had more money in our pockets we would spend it, which I do not conceive will always operate. The Townsend plan, for example, is of the same sort. There are several of our enthusiastic colleagues who have been addressing to us a great deal of literature about different plans of some sort, all with the purpose of giving money to people who have not earned it. Can any of those proposals, which violate the fundamental principles that you have mentioned, advance the common welfare?

Mr. **Spahr.** I should think that it would be one of the worst things the country could do, to do something of that kind.

Mr. **Luce.** That is all.

Mr. **Spahr.** There is no way to create wealth out of paper money.

The **Chairman.** There are two questions that I want to ask you.

Referring first to the difficulty that you referred to as obtaining in 1929, was there fear of inflation then?

Mr. **Spahr.** I should say no.

The **Chairman.** Would you say that that tended to cause that situation, or was it an entirely different matter?

Mr. **Spahr.** I should think it was a different series of causes.

The **Chairman.** You say that the way to increase consumption is by individual production, that that is the only way to increase production.

Mr. **Spahr.** At a profit.

The **Chairman.** You talked about profits later.

Mr. **Spahr.** I supposed that they all understood that, so I put that in as a correction.

The **Chairman.** You said that in 1928 the people overreached themselves. What did you mean by overreaching?

Mr. **Spahr.** Overproducing with respect to the existing market, piling up excessive inventories.

The **Chairman.** That is what I want to talk about. Do you mean that there was a greater production than human efforts and human happiness required?

Mr. **Spahr.** No.

The **Chairman**. You did not mean that at all?

Mr. **Spahr**. No.

The **Chairman**. And yet you say that increased production tends to bring about the desirable amount of distribution?

Mr. **Spahr**. Yes.

The **Chairman**. And, when production overreaches itself, there comes just the reverse of what you are talking about?

Mr. **Spahr**. Overreaches itself in certain important lines.

The **Chairman**. We talk mainly about food, and clothing, and shelter, do we not? And you had reference more to increased production of food products and clothing, than anything else?

Mr. **Spahr**. No. I had in mind the heavy industries.

The **Chairman**. You also had the others in mind?

Mr. **Spahr**. No; I did not. There is a fairly steady production and consumption of commodities of final consumption. You do not have a wide variation either in production or consumption of consumers' goods.

Mr. **Ford**. It was in 1927, was it not, when a very eminent professor wrote a book in which he pointed out that there were 20,000,000 people in the country who were living at below a subsistence line, and would you say that that was a kind of a drag such as might be caused by one of four-wheel brakes?

Mr. **Spahr**. To meet that, in part, they engaged, as you doubtless know, in installment buying to an excessive extent.

Mr. **Ford**. But the man whose income was below that level that they were referring to could not buy, whether you had installment buying or not. He had to go on a hand-to-mouth basis, to buy bread, milk, and 10-cent coffee.

Mr. **Spahr**. It is true that we had an incredible amount of installment buying during that period from 1927 to 1929. People went in debt beyond their capacity to pay, but that was just one device that producers were using to work their goods off onto the consumers.

Mr. **Ford**. But it was due to no lack of confidence in the Government or anything else. These things were going on, and there was no attempt on the part of the Government to regulate anything. We were sending billions of dollars to Europe without any regulation whatever, creating a very large foreign debt which we were paying for ourselves, and we were sending goods to Europe gratis, as it turned out, and then suddenly, without a word from anybody, things crashed. It was not a lack of confidence at that time at all. All of this parrying about lack of confidence, and all that junk, is just stuff that has been shot around here for the last 3 or 4 years by the opponents of the present administration.

Mr. **McKeough**. May I say right there that that was the year when we were all promised two chickens?

Mr. **Ford**. Yes; and there was no lack of confidence at all. Confidence did not enter into it. We were in a high productive period and all of the economic problems had finally been solved, and we were going into a new era, and all of a sudden somebody stubbed his toe and, bingo, we went into a crash.

The **Chairman**. I think it is fair to say this, that the plain truth is that these benefits spring out of fundamental actualities, and find their adjustment on that basis. It is like the market; I heard a man in a high place not long ago say that 100 men in New York would decide that they were going to advise their clients to buy on the market and then a little later they would say that the market was too high and would advise their clients to sell, and that man seemed to hold the view that there was not anything that could be done about it, that in this country everything was in the hands of a few speculators and it all rested with them, and that the only way you could get relief from that is to go up and kill them. I made the statement to him then that of course there were temporary conditions brought about by speculation within a speculative market. That is always true, but these things finally adjust themselves on a basis of actuality. In the stock market a man buys some stock, and some day he is going to see real value in it, and then he decides whether he will keep it or sell it or, if he does not have it, order what he wants to buy. The thing comes down to actualities sooner or later, and that was the condition back yonder, and when things went wrong, of course people began to lose and you had fear on your hands, but the condition of fear was the effect and not the cause, and I won't say, like Brother Ford, that all of your talk is nonsense, but we ought to know better.

Now, I want to make a suggestion. It is a quarter past 12, and there are several other controversial matters that I would like to take up tomorrow.

(After an informal discussion, off of the record, during which the witness was offered the opportunity of appearing at a later date satisfactory to him, the hearings on this bill were continued until Wednesday morning, February 9, 1938, at 10:30 o'clock.)

Prepared Statement of Professor Spahr, Continued

Section III (f): It is said that—

> the term "national credit" means the amount of national wealth against which money may safely be issued without resulting in inflationary price levels.

To define national credit as an amount of national wealth is to confuse concepts. National wealth is a national asset; national credit is a national liability.

The meaning of an inflationary price level is not made clear and until this is done the section is valueless. It is a simple truism to say that no credit should be issued that cannot be liquidated without loss; but the amount of credit that may be issued against a piece of wealth depends upon the price which that wealth will bring when the credit must be retired. Thus, under certain conditions any amount of currency could be issued against a given piece of wealth. For example, if a nation wished to issue paper money against national wealth, as France issued assignats and mandats against confiscated church lands, any amount of such currency could be issued, since the value of the property in terms of the paper money would increase as the value of the currency depreciates. Then it is to be remembered that even when a steady price level prevails, the situation often arises in which credit cannot be liquidated. Section III (f) reveals confusion of thought and can be of no value until clarified.

Section III (g): The definition of "national money" is vague despite the specifications. For example, this expression does not occur again in the bill, but the term "national currency notes" is used in title III, section 301 (a).

Section IV (a) does not specify whether the discount rate is to apply to preceding or succeeding months.

Section IV (b) suggests a discount rate at the start of 15 percent. It is doubtful whether the rate of profits for business, even throughout a decade of prosperity, would equal 15 percent on the average. Should it prove that under the proposed plan retailers would be discounting their prices by the full amount of their profits, this procedure would mean that the profits of retailers in the first instance would be shifted to purchasers in the form of lower prices, that the retailers in return would receive bank deposits equal to the discounts, that the banks would receive inconvertible paper money as assets against their increased deposit liabilities, that the banking system would become gorged with inconvertible paper currency, that the paper money liabilities of the Government would increase until perhaps national bankruptcy would occur. In short, this section provides the means of converting part or all profits of retailers into unsecured inconvertible paper money. There certainly is nothing that can be said in valid defense of this proposal.

Section IV (b), page 4, lines 2 and 3: It is impossible to measure "idle productive capacity" or "total productive capacity." And yet this plan provides that the discount rate of retailers shall rest upon the relationship between these two capacities. Not only are the concepts of these "capacities" vague, but just what the relationship between the two should be is not specified. The lines 3–5, say that "The method of arriving at these figures shall conform to the existing practice of establishing index numbers of trade." This is so vague in meaning as to be valueless.

Section IV (c) provides that "No retail discount rate shall be declared unless productive capacity, ascertained as above prescribed, shall exceed consumption by at least 15 percent." Statistically such a calculation is impossible of attainment. The most hopeful part of this section lies in lines 13 and 14, which provides that "after proclamation of this discount rate the data used in the determination thereof should be made a matter of public record." Certainly every economist would enjoy seeing those data, and we could be assured that conformity to the requirements of these two lines (13 and 14) would speedily terminate the experiment, should such a thing ever be tried here.

Section V, lines 4–6: Corporations, as consumers, are excluded from the provisions for the discount. But why should this be done if the purpose is to increase consumer purchasing power? What difference does it make whether the consumer be a corporation or a natural person? And how is a retailer to determine whether a product is to be used in business or for final consumption? For example, if a purchaser buys an automobile, he may use it for final consumption purposes on Sunday and for commercial purposes on Monday. The lines cannot be drawn as easily as implied in this bill between the final and intermediate uses to which many goods and services can be put. Or a purchaser may buy his radio or auto in good faith expecting to use it in final consumption, and yet later he may wish to trade it for a new model. But line 6 says he cannot trade or resell it. Such a provision should reveal its impracticability in the face of the practices of everyday life.

Section VI (a): This section subjects all retailers to licensing by the Secretary of the Treasury who could deprive any retailer of his license at will, thus forcing the retailer to go to court to protect himself. The burden of proof is thrown upon the retailer rather than upon the Secretary of the Treasury. This would make possible all sorts of abuses and favoritism. Or should the Secretary wish to administer the law impartially, he would be swamped with hearings. This provision would involve a tremendous bureaucracy, would inflict an unbearable burden on retailers, and would involve a degree of governmental meddling in business that would be undesirable from every point of view.

Section VI (b) has the same general defects. It provides for a governmental inquiry into costs of production and distribution to retailers that would require an army of Government agents equal to all the accountants now employed in business. Such a situation would be unbearable.

Section VII (a) provides that all banks engaged in interstate commerce shall accept these discount vouchers and create deposits against them. What banks are included? When is a bank engaged in interstate commerce, and when is it not? Who would decide this question? Are not all banks engaged in interstate commerce? And are banks other than commercial banks included?

Section VII (b) provides that the Secretary of the Treasury shall deliver to the approved banks interbank currency notes to a face value equal to that of the vouchers received by the banks. Although this currency is called an interbank currency and is to be used for clearing purposes to prevent its entering circulation (except as noted below) the effect is to make it more potent as an instrument of currency expansion than if it entered circulation directly. Its use releases other currency for reserve purposes, since reserves are now used for clearing purposes, and money used as reserves has the power of supporting greater currency expansion than currency entering circulation. Therefore, the suggested interbank currency has a greater capacity to support an inflationary currency expansion than if the currency went into circulation. Currency, other than Federal Reserve notes, cannot go into circulation without reducing reserves correspondingly. This interbank currency would in effect add to reserves thus enabling them to support additional deposits. The deposits which it represents would be the circulating medium. This provision, consequently, permits a currency expansion far in excess of the amount of such currency issued.

Section VII (c): It should be noticed that bank deposits are created against vouchers which are not promises to pay but merely a means of obtaining assets in the form of inconvertible paper money issued by the Federal Government. This plan provides for an inflation of bank deposits in a manner incomparably more dangerous than that involved in the creation of bank deposits against Government securities as assets. Government securities cannot serve directly or indirectly as reserves, and they are interest-bearing promises to pay that imply that the Government has serious intentions of redeeming them out of taxes in the course of time. The issue of this interbank currency is merely the Government's way of saying to the banks that they can use an inconvertible and unsecured paper as assets against deposits and to replace other currency which may be used as reserves. In this manner bank reserves are enlarged by being diluted with this type of paper. The probable consequences of such a procedure ought to be obvious.

Section 202 (a), page 10, lines 17–19: Here the Federal Credit Commission is charged with the duty of determining annually the value of the unusued capacity of industries and people of the United States. This could not possibly be done. It is further required that this is done with respect to "wanted goods and services." There is no possible way of measuring people's wants. These are unlimited and constantly changed.

Lines 20–22 read:

> **Each year the amount in the national credit control account which shall not have been drawn upon in that year shall be written off.**

These lines convey no clear meaning. Preceding lines say that the value of the unused capacity of industries and people shall be credited to the national credit control account in the Treasury of the United States, but this entire section 202 (a) is too vague and nebulous to be interpreted or reduced to anything concrete. As a matter of fact, the bill contains no provision as to the purpose that the national credit control account is supposed to serve.

Section 203 would have the effect of removing the National Credit Commission from any criticism whatsoever. No one could criticize it without violating the law. Such a situation would be intolerable in a democracy.

Title III, section 301 (a) deals with interbank currency notes without specifying their nature. There is no reason to suppose that they are anything but an unsecured and inconvertible paper currency.

Section 301 (b) provides that these interbank notes, which may be issued to the extent of billions of dollars, "shall constitute a revolving fund for the stabilization of domestic trade by maintaining purchasing power in the hands of the public through the adjustment of the retail price level and so as to avoid undue expansion and inflationary conditions." What does adjustment of the retail price level mean? What would be undue expansion under this scheme? Instead of providing against inflation, the plan guarantees it.

Section 301 (d) provides that interbank currency notes may be used by the banks as reserves, "dollar for dollar, but not as a medium for expanding private credit in the form of loans built on fractional reserves." This merely means that the banks may utilize this inconvertible paper currency as reserves against the deposits growing out of the discount vouchers. But since this currency cannot be paid out, it is not a reserve in fact, and the burden of the deposit liabilities is thrown on the other reserves. Thus this section is confusing in the use of the word "reserve." But in subsection (h) it is provided that these notes may be converted into "national currency notes" (whatever these are), and that the latter may be paid out to customers. By a little juggling, by substituting one inconvertible paper money for another, a paper money that is called an interbank currency in one part of the bill, and a "bank reserve" in another, can be paid out as circulating cash when bank reserves are otherwise depleted. Lines 9–15 of subsection (h) say that the banks which have paid out these national currency notes shall proceed "with the orderly realization of their reserves and the curtailment of their outstanding credits until they are able to restore the national currency so borrowed and reestablish the circulating credits previously established by the interbank currency notes held by them." What does "orderly realization of their reserves" mean? And how shall outstanding credits be curtailed? Shall these banks refuse to accept the discount vouchers which section VIII (a) directs them to accept? Shall other types of loans be called and refused? What circumstances would bring these notes home after they have entered circulation? The provision for the retirement of these national currency notes is vague indeed.

Section 301 (e) provides that—

> **upon the findings and advice of the Federal Credit Commission that inflationary conditions are tending to arise, the Secretary of the Treasury is hereby authorized and instructed to recall from the banks such amounts of the interbank currency in their hands as may be necessary to establish and maintain monetary equilibrium.**

If the Commission fulfilled its function intelligently it would find that inflationary conditions were arising the instant this interbank currency was issued and would, therefore, recall it at once.

But the recall of such currency, as provided here, wold not reduce the banks' deposit currency in circulation; it would merely reduce the banks' assets, or reserves if this type of currency is really part of the bank reserves. And what would the Commission return to the banks in exchange for the currency retired? That important matter is overlooked here. Finally, what does "monetary equilibrium" mean?

Section 301 (f) is a partial attempt to answer the preceding question as to how the interbank currency is to be contracted, and provides that the bank shall promote an orderly liquidation in order to permit a return of this interbank currency. It is clear that the deposits resting upon the discount vouchers cannot be liquidated; therefore other loans must be liquidated. It is also provided that Government securities shall not be sold if this act tends to depress their prices; thus again the burden is thrown upon legitimate loans. In short, this section proposes to force the banks to penalize legitimate loans and business with great severity, while leaving the inflated deposits undisturbed. In other words, only the legitimate deposits growing out of legitimate loans would be contracted, while deposits resting upon Government securities and discount vouchers would remain outstanding. If one were to set about purposely to devise a scheme to guarantee a perpetual inflation of the currency, a squeezing of legitimate business, and a depletion of sound bank reserves, it would be difficult to improve upon the devices provided here.

Section 301 (g) provides among other things that, despite the preceding provisions of the bill, nothing in it shall be construed to prevent the use of open-market operations in Government securities. If banks cannot sell their Government securities when their prices are falling, of what value would the open-market operations of the Federal Reserve banks be? This section also provides that the Board of Governors of the Federal Reserve System shall have the power to institute a 100 percent reserve scheme, the nature of which is not explained, but which, as thus far advocated in this country, is inflationary in nature, since it involves a proposal to substitute inconvertible paper money for the banks' assets. It is clear at once that the proposals in this bill conform to the principles of the 100 percent reserve scheme as commonly advocated, although the approach is indirect.

Section 301 (h) has been discussed above in another connection.

The bill is replete with punitive sections, and a closing section (404) provides a blanket repealer which characterizes legislation of such a loose character that the bill drafter does not have the enterprise to determine what preceding laws are or are not repealed. He leaves that worry to the private citizen, the administrator, and the courts.

This bill has no virtues whatever, merely fallacies and dangers, and it requires no small amount of self-restraint to terminate the comments upon it by simply saying that the Banking and Currency Committee and, if necessary, Congress should not have the slightest difficulty in understanding the proper action that should be taken with respect to it.

These comments have not been made without a knowledge of Representative Goldsborough's interpretation of the bill as set forth in his speeches in the House of Representatives on June 8, and July 9, 1937. It is recommended that those speeches be read for some insight into the author's money and banking theories, and for such additional light as they throw upon the purposes and theories involved in the bill under consideration.

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

WEDNESDAY, FEBRUARY 9, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings were resumed on H. R. 7188 at 11:01 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. Evans, Mr. Transue, Mr. Barry, Mr Fish, Mr. Gifford, Mr. Luce, Mr. Crawford, and Mr. Gamble.

The Chairman. The committee will come to order, please.

We have with us this morning Mr. James H. R. Cromwell, who has had wide business experience, especially in the industrial field in connection with automobiles, and who is interested in finance and economics. He will now discuss this bill; and I am sure, Mr. Cromwell, that the committee will be glad to hear you.

STATEMENT OF JAMES H. R. CROMWELL

Mr. Cromwell. Mr. Chairman, may I ask that there be no questions until I complete my statement?

The Chairman. Do you have a written statement?

Mr. Cromwell. Yes, sir; and I ask that I be permitted to complete the reading of it before the members interrupt me.

The Chairman. I am sure that you may do that.

Mr. Cromwell. Thank you, sir.

Allow me to state immediately that I wholly coincide with and approve of the economic objective which Mr. Goldsborough's bill (H. R. 7188) seeks to achieve. My associate, Mr. Czerwonky, and I are appearing before this committee for two purposes: First, to clarify the objective of Mr. Goldsborough's bill; and, second, to suggest what we believe might be improvements in the methods proposed by Mr. Goldsborough to achieve the purpose he has in mind.

The purpose of Mr. Goldsborough's bill is to expand national purchasing power; that is to say, to add new dollars to our economic system as the flow of finished consumer goods increases. Now, this objective, I am sure, at once raises two major questions in the minds of the committee: First, why is it necessary to add new dollars; and, second, what is the justification for adding new dollars? In other words, on what grounds, on what basis, are these new dollars added, and what is behind them? What, in substance, would prevent inflation and keep our billions of nebulous credit money virtually stable in purchasing power?

I believe those are the questions in the minds of the committee that the members would like to have answered.

To answer these questions in simple and easily understood terms I shall turn back to a primitive capitalistic economy and try to develop from this fundamental foundation, step by step, a clear picture of the complex corporate superstructure of modern capitalism. Let us imagine, therefore, a primitive economy wherein the producers of various essential goods, in order to facilitate the exchange of their goods and services, set up a trading post which would be given the power to issue money tokens in exchange for goods. On the first of the month Shoemaker Smith brings in a pair of shoes and is paid five tokens, Farmer Ford is paid five tokens for a sack of flour, Hatmaker Harris five tokens for a hat, Tailor Thomas five tokens for a pair of pants, and so on.

As a result of these payments the shelves of the trading post are filled with goods, and its till is empty of tokens. The recipients of the tokens, in the meanwhile, have begun to use them to pay for services rendered by other members of the community who are not actual producers of finished goods ready for consumption. Dentist Drew and Physician Phillips, for instance, are given tokens by Farmer Ford and Shoemaker Smith for personal services rendered.

Since every one of us eventually must obtain finished consumer goods in order to live, let us assume for the sake of simplicity that by the end of the month all the goods on the shelves of the trading post have been bought and paid for, that is to say, claimed by the tokens issued so that the shelves are empty and the till is full. Thus, in this primitive economy, each month, the process of producing and consuming goods is repeated as described. And here we have a clear, though elementary picture, of the same productive-consumptive process or cycle which is going on at this moment in our complex economy of today. Here, in this primitive trading post, is an ideal illustration of the inseparable relationship which exists between goods and money. Here, each month, in our mind's eye, we can visualize the flow of money and the flow of finished consumer goods passing through the trading post in perfect balance, or as I term it, perfectly synchronized.

Now, the first lesson to be learned from this oversimplified illustration is that tokens, which we call dollars, can only be issued against finished goods ready for consumption. If, for instance, Farmer Ford brought in a bag of raw wheat to sell, nobody would claim it because nobody could use it until it had been ground into flour. Of course, the point I am making is that the trading post cannot issue tokens against anything except finished consumer goods. I do not mean to imply that individuals within the community are restricted to finished consumer goods in the use of their tokens. Shoemaker Smith, for example, might use some of his five tokens to buy a cowhide from Farmer Ford but such exchanges of goods in varying stages of processing, or the transfer of tokens for services rendered, would have nothing to do with the trading post. The number of times or the rapidity with which its tokens changed hands would not affect the trading post so long as all the tokens issued ultimately were used to claim all the finished consumer goods on hand.

In other words, the sole responsibility of the trading post is to see that there are always enough tokens issued to claim all of the finished consumer goods on its shelves. So long as this responsibility is fulfilled our imaginary primitive economy will remain balanced and stabilized, irrespective of the velocity or speed with which members of the community use these tokens between themselves to exchange services or unfinished goods. The only measure of the velocity of money which means anything, therefore, is the time that is required to complete the cycle of the production and consumption of definite quantities of finished consumer goods.

If this relationship between goods and money is applied to our modern economy it will become clearly evident that the number of times or the speed with which dollars are exchanged between individuals for pieces of paper such as security certificates or in other intermediate transactions should not affect the production and consumption of goods, which is all that really matters.

So far I have, of course, been dealing with a stationary or static economy in which living standards were not rising nor population increasing. But population does increase and living standards do rise, so let us see what happens in our imaginary community as more goods are required. Let us assume that the manager of the trading post tells Farmer Ford that there is no longer enough flour to go around and suggests that Farmer Ford clear off another acre and double his production of wheat.

By working overtime Farmer Ford, therefore, doubles his production and eventually brings in to the trading post two bags of flour instead of one. Now, isn't it obvious at this point that the trading post, having previously paid five tokens to Farmer Ford for one bag of flour, must now issue five new tokens to pay for the second bag? Isn't it obvious that if the trading post did not issue additional tokens as additional goods were produced that there would be no purpose or incentive for Farmer Ford to grow more wheat? Isn't it obvious that the price of Farmer Ford's flour would be cut in half if he received the same number of tokens for twice the quantity of flour?

So the second and third lessons to be learned from our imaginary primitive economy are: (A) that the flow of dollars must be increased as the flow of finished goods increases; and (B) that only permanent increases in the flow of finished consumer goods justify increases in the number of our dollars. Goods ready for immediate consumption, therefore, represent the only genuine backing which can be "behind" our dollars and not an accumulation of gold, silver, or other metals. I submit that since the ultimate purpose of dollars is to facilitate the production and consumption of finished goods that any so-called backing other than goods is purely fictitious and synthetic.

Now, before we proceed to develop our primitive community into modern capitalism, let me use it to illustrate still another lesson. That is the lesson of hoarding. Let us suppose a member of our imaginary community hides one of the tokens he has received in his sock instead of taking it down to the trading post and using it to claim goods. What is the result? The trading post will, of course, have a modicum of goods left on its shelves. But the serious fact is that when producers bring in their usual quota of goods the post will be short one token with which to pay them. Some producer, under these circumstances, would not be able to sell all the goods he has produced and there would then be both overproduction and underconsumption in our imaginary community. Obviously, therefore, the trading post, in order to maintain the balance of the productive-consumptive cycle, would be compelled to replace or offset the missing token. The fourth lesson, therefore, is that the flow of dollars must be compensated to offset hoarding.

At this stage of my illustration our imaginary economy has begun to grow and expand but is still primitive in character because I have assumed that all production was carried on by individuals or families. But let us now advance to corporate or collective capitalism by assuming that Farmer Ford's wheat acreage has increased to such an extent that there is not only an abundance of flour in the community but that Farmer Ford is no longer able both to cultivate his wheat and mill it too.

Farmer Ford's son Fred is an enterprising young man and decides that it is time to build a mill just to grind wheat for the community. But if Fred stops growing wheat and ceases to produce while he is actually building the mill, he could not earn any tokens to buy goods to provide himself with food, clothing, and shelter. To secure the necessary tokens, therefore, he persuades others in the community each to lend him a few of their tokens in order that the productive facilities of the community may be increased, although by so doing they sacrifice part of the goods to which they are entitled. In return for this sacrifice, which we call thrift or saving, Fred agrees to compensate them by paying each investor in his mill, say, one-twentieth of a token every year.

Naturally, Fred has figured out how much in tokens his wheat will cost and what price he can get for his flour. The solvency of Fred's mill therefore, assuming he is an intelligent enterpriser, depends upon the relative stability of the price of wheat and flour. If the trading post fails to increase the number of tokens as the flow of flour and other finished goods increases, fewer tokens will buy more goods than formerly; that is to say, the price of flour will fall. If the price of flour falls too far Fred's calculations will be wholly upset, and he will find himself unable to operate the mill at a profit and will shut it down.

So now our imaginary primitive economy has evolved into a modern corporate system of capitalism wherein enterprises, like Fred, manage great mills and factories for the purpose of earning a profit for their investors or stockholders. Unless profits are earned investors naturally won't invest and labor cannot be employed. Moreover, these corporations of today, great and small, are laced in a strait jacket of virtually rigid costs payable in dollars. Rent, interest, taxes, insurance, and so forth must be paid in fixed sums of dollars, and so it is obvious that when the flow of dollars becomes inadequate and prices fall, these corporate entities cannot obtain enough dollars from the sale of their products to meet their costs plus a reasonable profit. To repeat, if corporations do not earn a profit labor cannot be employed.

In our capitalistic economy of today there is, of course, no such thing as a trading post; goods are distributed from millions of different outlets, and we have thousands of banks of issue. Yet the fundamental principles are the same and can be applied to our complicated modern system as readily as to our imaginary primitive system. The number of marketing outlets or banks of issue is immaterial provided we establish a central agency which is directed and equipped to see to it that the flow of dollars springing from our thousands of banks of issue is, in the aggregate, synchronized with the flow of finished consumer goods distributed by our millions of marketing outlets.

Nobody will deny that the flow of our dollars actually has increased since 1776, in relationship to the increased production of the Nation, and it is my belief that this depression and other so-called business cycles which have afflicted our country almost every decade since the Revolution, are attributable to the fact that the necessity for synchronization has never been recognized and that the flow of dollars has been expanded and contracted without any regard to the flow of goods. I submit, furthermore, that economic stability, capacity production, and full employment in the United States will never be achieved until a central agency is established whose responsibility shall be to synchronize the flow of dollars with the flow of finished consumer goods in order that commerce, as a whole, may be conducted at a profit.

And now, gentlemen, I will try to substantiate my statement that the fundamental principles illustrated by the primitive economy are entirely applicable to our economy of today by applying these principles to three dynamic charts which represent the functioning of our modern corporate system of capitalism. First, however, let me explain that since our capitalistic system of today is a living, growing organism in constant motion, these charts represent merely snapshots of our system taken at any given moment. I contend that it is just as futile to attempt to explain the functioning of our economic system by segregating for analysis specific amounts of money or goods, as it would be to explain the functioning of the human body by analyzing specific amounts of blood.

Chart 1 shows our economy at the ebb tide of a depression. The Nation, in other words, is at a standstill; the flow of dollars and goods is neither being expanded nor contracted. The outer circle represents the flow of goods and the inner circle represents the flow of dollars carrying these goods between producers and consumers. The two circles are analogous to an automobile wheel and a tire and the effect, should one part shrink or expand in size without the other, would be equally disastrous in both cases.

At point B we may assume that raw commodities are being received and are being processed into finished consumer goods between points B and A. At point A they are being marketed by retail outlets and from A to B are being consumed. The inner circle, of course, represents, from B to A, producers paying out dollars for raw commodities, rentals, wages, and so forth, and receiving back these dollars from A to B.

The number of times and the speed with which these dollars may change hands during the complete productive-consumptive cycle is immaterial, for the vital point is that, like the primitive economy, there must be sufficient tokens issued to absorb the goods on the shelves of retail outlets.

Chart 1 likewise illustrates the fact that taxation has no effect upon the current flow of dollars, and therefore is not an instrument which can be used to prevent or cure depressions resulting from unbalances between the flow of money and the flow of goods. Of course, it is obvious that when taxes are heavy there will be more people who produce nothing but who nevertheless must share in the total quantity of goods produced.

Chart 2 shows the turn of the tide and our economy coming out of a depression and once again beginning to expand. It illustrates, furthermore, two vital factors: First, how the investment of savings or capital expands the flow of goods without changing the flow of dollars. Second, how taxation of capital, such as income and estate taxes, curtails the expansion of production.

At point B we see the dollars of investors in double action. Here their dollars are exchanged for the securities of new or growing corporations, and simultaneously production is expanded and the dollars of the thrifty are paid out to workers engaged in building new facilities. As in the example of our primitive mill builder, Fred Ford, these dollars are used by the workers creating the new productive facilities to claim the goods which the thrifty denied themselves. Please note how the investment pipe line diverts dollars to the expansion of production and subsequently returns them to the main stream of purchasing power. At point B the expansion of production is illustrated by the increased size of the goods flow circle extending halfway between B and A. This signifies that the new facilities are only half completed, and that the flow of finished consumer goods at point A has not yet been increased.

So far as the investment pipe line is concerned it is clearly evident that high taxation of actual and prospective investment capital constricts the flow of such capital and thus proportionately curtails the expansion of production, reduces the demand for labor, and is therefore detrimental to the national standard of living. This fact is more clearly illustrated by chart 3.

Chart 2 shows our economy at the high tide of such prosperity as should in this Nation be normal. Here we find that the new productive facilities started on chart 2 have begun to deliver an increased flow of finished consumer goods at point A, the market place. We see at once that the tire has expanded in size whereas the wheel has not.

Since we have no trading post responsible for increasing the flow of dollars in proportion to the increased flow of goods, it is obvious that unless dollars happen to be increased by mere fortuitous circumstances, we will have more goods than dollars. The inevitable result will be a decline in prices; business will become unprofitable, labor will be discharged, wages will be cut and depression will set in. This is the "bottle neck" or "hot spot" of modern capitalism, and I contend that failure to recognize the vital necessity for increasing the flow of dollars at point A is the determining cause of our so-called business cycles and depressions.

I urge, therefore, that the Board of Governors of the Federal Reserve System be directed and fully empowered, not only to increase the flow of dollars as required by increases in the flow of finished consumer goods, but to offset as well any hoarding which might take place. I contend, in other words, that the Board, or some other central agency, must be given a mandate and must be equipped with positive means to synchronize the flow of our dollars with the flow of our finished consumer goods.

Now, Mr. Goldsborough's bill, H. R. 7188, provides positive means to achieve synchronization; and as I said at the beginning of my statement, Mr. Czerwonky and I are prepared to comment on these means and to suggest other methods of synchronization which, in our opinion, would be equally effective and less difficult to administer. Unless, however, the majority of this committee are now familiar with what synchronization represents and are convinced that it is essential, there is no purpose in wasting the committee's time by explaining the positive monetary means by which we believe it can be attained and maintained. I realize, Mr. Chairman, that synchronization is a new and startling economic theory, and if the committee desires to obtain further information by questioning me, my time is at your disposal.

The **Chairman**. I think that you are in slight error in assuming that the members of the committee have not become acquainted with this theory of synchronization, as you defined it. We have heard experts over a period of years on this and other subjects, so it is not new to the members of the committee; but, in any event, I am sure that the committee will be delighted to hear you expand your thought, and to hear any plan that you have in mind designed to accomplish the objectives that you desire and that, I am sure, all of us desire.

Mr. **Goldsborough**. Right in that connection, in the bill which is now under consideration, the Federal Credit Commission is the trading post. You have a system which you think would be more effective and simple than that, and I would like to have you proceed along that line and to explain your plan.

Mr. **Cromwell**. Well, I wanted to be certain that all of the members of the committee understood the necessity for these positive methods, Mr. Goldsborough, and to find that the majority were agreed that synchronization is essential in our modern community life.

The **Chairman**. I think that that is entirely true, but, stating the matter bluntly, the committee would be glad to have you tell us what you would do, or have done.

Mr. **Crawford**. Mr. Chairman, may I ask him a quesion?

The **Chairman**. Mr. Crawford.

Mr. **Crawford**. Mr. Cromwell, if the plan that you have suggested were put into operation, could the production of goods be controlled satisfactorily, do you think?

Mr. **Cromwell**. Do you mean, would there be likelihood of overproduction?

Mr. **Crawford**. Yes. In other words, how would you control overproduction if it should begin to take place, as we understand overproduction today? Using our usual terminology, how would you control overproduction?

Mr. **Cromwell**. In other words, your thought is that if we continue to increase the flow of money as the flow of finished consumer goods increased, where will production stop; where will there be some control over the possibilities of overproduction? Is that right?

Mr. **Crawford**. Yes.

Mr. **Cromwell**. I anticipated that that question would be asked by some member of the committee, because that seems to be a natural reaction, the first reaction to these charts, and we have therefore prepared an answer to that question, because I believe that the matter of overproduction is the usual question that comes into the minds of those who see this theory of synchronization as——

Mr. Crawford. It is very often claimed that that was largely the cause of our trouble in 1929.

Mr. Cromwell. That is quite true.

Mr. Luce. Would Mr. Cromwell prefer to finish on the first part of his discussion now, before I ask a question which perhaps he contemplates covering later?

Mr. Cromwell. I was anxious to have any questions on this theory of synchronization asked me by the committee before I pass on to the positive central bank mechanism by which we believe that this theory of synchronization can be made effective. In other words, I wanted to divide the subject into two distinct parts, because it really is divided into two distinct parts, one the theory of synchronization. Is or is not synchronization necessary? If we agree that it is necessary, the second part would be the specific and positive central bank mechanisms by which synchronization could, in our opinion, be made effective.

Mr. Crawford. Would you also prefer to defer the answer to my question until some later time?

Mr. Cromwell. That would be entirely satisfactory; whatever is the pleasure of the chairman and the committee. This is a very short answer, and I can read it quickly.

Mr. Fish. There is no reason why you should not do it now.

Mr. Cromwell. I would prefer first to answer Mr. Crawford's question, and then go to whatever question Mr. Luce has in mind.

Mr. Crawford has asked the question, What would prevent overproduction so long as the Board continued to issue new money to offset additions to consumer goods flow?

Now, the answer to this question must be divided into two parts, general overproduction and specific overproduction.

First, as to general overproduction. We know that new production is rendered possible by the abstention from spending of savers and that such thrifty people expect and are entitled to a just reward for their self-denial. We also know that the reward is paid to them in the form of dividends and interest. Now, if savers invested too much and consumed too little, earnings would gradually decline and savers would naturally be inclined to invest less and consume more. General overproduction, therefore, would be impossible under a scientific money system, because the see-saw of thrift versus consumption would automatically balance the economy as a whole.

Second, as to specific overproduction. Let us assume that automobile production reached the point where we had two cars in every garage and there was no room or use for a third. In this case the production of automobiles would tend to become stationary because both savers' and consumers' dollars would flow to other goods—like air conditioning, aviation, television, et cetera—where both demand and profits would be greater.

It is important to understand that there is a complete difference between a specific industry becoming stationary and being overproduced. As an industry gradually tended to become stationary, its ratio of increased production would decline as compared with the average of former years. For instance, in 1936 the automotive industry might show a 15-percent increase in production as compared with some basic year such as 1930. In 1937 the increase might drop to 10 percent, in 1938 to 5 percent, and in 1939 there might be no increase whatever. In other words, the industry in 1939 would have become stationary. But it would not have been overproduced—there would be no cut in production, no discharge of labor, and no decrease of any kind—there simply would be no increase.

Since the Board could issue new money only against an increase in our national flow of finished consumer goods, it stands to reason that if our whole economy should become stationary no additions in dollar flow would take place and the economy would therefore remain fixed in perfect balance. Demand for specific goods in the future will doubtless decline or shift to other types of goods, just as has occurred in the past, and new inventions and altered habits and desires will always engender possible overproduction and wastage in some specific industries and underproduction and shortage in others. These very factors, however, stimulate competition and new production, so that capitalism, freed from the shackles of an uncoordinated system of distribution, would be spurred on to an even more amazing era of progress and development than was witnessed by the last century.

Mr. **Crawford.** Where you referred to the economy being fixed and in perfect balance, do you mean to say by that that if this monetary control were in operation it would guarantee the sale of all goods at a profit?

Mr. **Cromwell.** I would like to answer that question with a prepared statement.

I do not mean to create the impression that adjustments in dollar flow will make the sale of all goods profitable. The managers of an enterprise may produce an article which does not appeal to consumers, and because of this they may not be able, in the sale of the given article, to recover the money costs involved. Stockholders of such enterprises naturally suffer a loss; and this element of chance is of course always present in all business enterprises. The element of economic chance is, and will remain, part and parcel of the profits system because it is a system in which the free selection of goods prevails.

So far as natural economic chance is the cause of unprofitable business activities, complaints by the management and stockholders of American industry obviously are unjustified. However, when such risks are artificially magnified by failure of our monetary authorities to make, or induce, such adjustments in dollar flow as will counteract increased finished consumers' goods flow brought about by the combined actions of the savers and managers of industry, then American business enterprisers, stockholders, and workers in industry have cause to complain and to demand that positive methods be provided to correct this physical defect.

It must be repeatedly emphasized that the free play of competitive forces will not in itself enable the profitable absorption of an increased flow of finished consumers' goods brought about through the combined actions of savers and business enterprisers, nor will such a policy assure the continued full utilization of our productive capacity. The man-made institution of money must be made to adjust itself to the new economic conditions.

Mr. **Ford.** May I ask a question there?

Mr. Cromwell, in your original statement you used a phrase "billions of nebulous credit." You used that phrase advisedly, I assume. Do I understand by that that under the present system, whereby a man borrows from his bank, for instance, to produce 1,000 tractors, and he needs the money for raw material, labor, and all of the other expenses involved in the production, when those tractors have gone into consumption then he gets his money back, usually, as they are sold over a period of 2 or 3 years, for the farmer buys them on the installment plan, but his loan at the bank is usually for 90 days or 120 days, or they may renew the loan a half a dozen times, but unless he has almost unlimited credit there comes a time when that note has to be paid, and it is paid in advance of his collections, and of the original, we will say, $300,000 that he has on his books from these purchasers, his loan was probably $100,000, and he has only $75,000 back, so he has to borrow from his normal capital $25,000 to clean up that loan.

Is that the kind of credit you were referring to as nebulous credit, that comes and goes, and disappears the moment the loan is called?

Mr. **Cromwell.** Yes, Mr. Ford; it is the kind of credit that has to be renewed.

Mr. **Ford.** Just at that point, what are you going to substitute for it? What is your plan of substitution? I think that that is the crux of what we are getting at.

Mr. **Cromwell.** That would come under the second part of the discussion, as to the positive methods that we would recommend.

Mr. **Ford.** Can you indicate in just a word or two what you have in mind?

Mr. **Cromwell.** I would prefer, Mr. Ford, if it is agreeable to you, to go into the methods tomorrow, after I have finished with any questions on this theory of synchronization, and I am anxious, Mr. Ford, to do one part at a time. I think that you will obtain an answer to your question tomorrow, after I have explained the methods by which we propose to maintain the flow of what I call our nebulous credit.

Mr. **Ford.** I am assuming that the flow that you attempt to regulate, and that you are going to explain, is something different from what Mr. Goldsborough had in mind? He would supply that through this discount and interbank currency. You have another plan?

Mr. **Cromwell.** Yes, sir.

Mr. **Ford.** Then we will get that tomorrow. All right.

Mr. **Luce.** It is possible that I may be anticipating what you are going to say tomorrow, Mr. Cromwell, but inasmuch as in your first statement here there is a reference to, and the argument is built on the basis of, tokens, which we commonly call cash currency, I would inquire whether there is not another element that must be brought in there at the same time with it.

I had read that 92 percent of the transactions in this country are achieved by the use of checks, and I had the curiosity to analyze my own expenditures for 12 months, and found that exactly 92 percent was accomplished by the use of checks.

Now, these checks are based, in part, upon credit. The banking system exists to manufacture credit, and, if I understood correctly, the volume of outstanding credit depends, like in all other business transactions, upon demand and supply. You gave an illustration of one man who hoarded a certain token, and in our system the trading post can, by the use of the credit system, put in a token, and I would like to have you make clear to me why in the present system, where credit adjusts itself to the demands of business, there is need for any artificial subsidy?

Mr. Cromwell. Well, I have endeavored to show in this chart here that there must be a positive means to see to it that the flow of money, and, of course, Mr. Luce, when I speak of money, I am really speaking of the 92 percent, the bank credit which you have mentioned; that is what I really mean by money, because we both recognize and realize that the currency of the Nation plays a comparatively small part in the business transactions, and the reason why, in the elementary, primitive example that I gave, I used a token, was merely for the sake of simplicity. You realize and I realize that those tokens could have been book credits just as well as actual pieces of paper or coins, whatever they may have had in that primitive day. The example would still have been just as good if we had assumed that the trading post maintained books and never paid anything out.

Mr. Transue. Mr. Cromwell——

Mr. Cromwell. I have not yet finished with Mr. Luce, Mr. Transue.

You asked, Mr. Luce, why we require that positive means be given to a central agency when it may be assumed that our credit institutions will make up additional funds as additional goods are presented to the market.

Is that about the question that you have in mind?

Mr. Luce. Yes.

Mr. Patman. Will Mr. Cromwell be back tomorrow?

Mr. Cromwell. Yes.

Mr. Patman. We have a very important matter coming up at 12 o'clock, and I would like to be there.

The **Chairman.** We have a few minutes left.

Mr. Patman. I just wanted to make sure that he will be back tomorrow.

Mr. Luce. What I am after is to have you tell me why the present system of meeting the business needs is not adequate, in view of the fact that the lendings of the banks fluctuate up and down from time to time in instant response to the demand for money?

Mr. Cromwell. Well, that is a matter, as I say, of fortuitous circumstance. The banks may be willing to lend, or they may not be willing to lend. The same with a borrower. The borrower may wish to borrow, or he may not wish to borrow. In case, I say, those circumstances should occur, then there would be no increase in the flow of money, but our system would immediately become unbalanced. Therefore I say that there must be some central agency which is instructed positively to see to it that there shall take place an addition in the flow of money. We cannot leave it up to the state of mind of the individual banker and the borrower. We must be certain that the flow of money is increased.

Mr. Luce. That doctrine is to be found in very many of the things that we are doing here in Washington today. The papers are full of compelling our lenders, if possible, or bribing our lenders to advance money for housing, for example. For a century, just about, the checking system and the credit system seemed to me to have met the law of demand and supply completely, except, of course, in instances of great fear, as in a panicky or depression period; but normally, through the years, demand and supply have proved adequate, and why should we adopt some artificial device in trying to amend the law?

Mr. **Cromwell.** I can answer that question in another way. I have tried to show by these charts, particularly chart 2, Mr. Luce, that the increase necessary in the flow of dollars is brought about through the flow of investment in the new undertakings, and that as this flow of goods increased, due to the saving process within the Nation, it then becomes necessary in the chart, at point A, to increase the flow of dollars.

Now, according to our gold-standard system, the savings process within the Nation has absolutely nothing to do with the flow of dollars. That is fixed by a definite and arbitrary quantity of gold. Consequently, when through the savings process within the Nation we bring about an increased flow of finished consumer goods, and this figure is continually building up, we have a fixed amount of gold in our system, and when the banks reach a certain period of expansion of credit, they say, "Well, we cannot expand any more, because we have not enough of this metal buried in the ground."

Mr. **Luce.** Well, now, Mr. Cromwell, you are anticipating a situation that has not existed for years. At the very moment, the banks are hunting for places to lend money and lacking in private demand. They are lending to the Government many, many, many millions of dollars which would be available for private lending, and which is not likely to disappear. At the moment, anyhow, there is no demand for an artificial addition to credit resources.

Mr. **Ford.** Might I make a comment at that point?

I just had word from California that, following the passage of the F. H. A., the banks are simply swamped with applications for loans for houses. They are wiring me to send them the regulations by air mail, so that they can meet the demand.

Mr. **Luce.** I am not surprised. I never yet saw a situation where, when men who have no means or resources, nor any character, are encouraged to borrow money, they did not come up by the thousands. That is apart from this particular question. I am trying to find out why, at the moment, there is any occasion to furnish additional currency, either cash or artificial.

Mr. **Cromwell.** I would say that one very good reason is that the statement of the Board of Governors of the Federal Reserve System shows that our demand deposits within the past year have decreased by over $1,000,000,000. Now, we cannot assume that the flow of goods has decreased. There is no reason why it should.

The **Chairman.** We are told that in 1929 there was a turnover of $100,000,000,000 of bank credit in the United States, and we witnessed a decline that represented a loss of half of that turnover. If half of the Government currency, which we call gold or silver currency, had at that time vanished or been destroyed or lost at sea, without any comparable change in the production of goods or products of the United States, everybody would have recognized that there had been a maladjustment that called for correction, and that is really what happened, and that is what you say should be corrected. You say that we should have some kind of a system that will adjust the supply of currency, whatever it may be and in whatever form it may be supplied by the Government, and that there should be some control or method by which the supply of that credit will not be subject to the vicissitudes of trade and the things that enter into the minds of men who have control of that kind, primarily for the purposes of profit, and that there should be a control that will insure a satisfactory adjustment of that currency to the production of the Nation and the demands of the public for goods produced—that is what you are aiming at, if I understand you.

Mr. **Cromwell.** Yes, sir.

The **Chairman.** I think we all agree that that needs to be remedied, and I think that one thing now that prevents the resumption of the use of bank credit in the United States is this state of mind that has not yet been relieved since this period of abnormalcy came upon us a few years ago. Maybe in the course of time the banks and the individuals will decide that the time has come when they should begin again to employ credit and to make use of it as currency, and to build it up to the point where it would meet the production and the demand for goods, and maybe for a time it would operate again and bring about a resumption of satisfactory conditions, but evidently the inherent weaknesses and difficulties that have brought about our troubles in the past are still inherent in the system, and need adjustment in some way.

I did not mean to talk that much, but that seems to be what you have in your mind.

Mr. **Luce.** Will you permit me to say that that is a very fair statement that you just made, and I do not take issue with you on that at all.

Mr. **Gifford.** May I make one suggestion?

Having in mind the present doctrine of subsidized scarcity by B, and the tremendous amount of money pumped over to A, at the moment your theory is in direct contravention with that of President Roosevelt, is it not?

Mr. **Cromwell.** Yes, sir; Mr. Gifford.

Mr. **Gifford.** And the Government is doing exactly what I stated, is it not?

Mr. **Cromwell.** It is constricting the flow of capital into industry. There is no doubt about that.

Mr. **Gifford.** It subsidizes scarcity—isn't that right?

Mr. **Cromwell.** I would not say it was subsidized.

Mr. **Gifford.** Apparently the plan you present is not at all in harmony with the present movement.

If you do not know what I mean by subsidized scarcity, sit in the gallery this afternon.

Mr. **Goldsborough.** I think the witness came here to be constructive.

The **Chairman.** He will take care of himself.

Mr. **Goldsborough.** To require him to criticize some action of somebody else I do not think is fair.

Mr. **Gifford.** No; that is not a fair statement by you at all.

Mr. **Cromwell.** I want to answer your question. Would you tell me exactly what you mean by subsidized scarcity?

Mr. **Gifford.** To keep land out of production, so that they will not produce.

Mr. **Cromwell.** Yes, sir; I would say that that policy is contrary to the idea of synchronization, which, of course, encourages or means to encourage the flow of capital into industry, so that the production of the Nation shall be increased and when the new finished consumer goods come on the market, there shall be an agency which will see to it that there is sufficient new money.

Mr. **Gifford**. You realize the amount of money that has been pumped into the soldiers' bonus, and into other gifts. How would yet get those gifts into the hands of the consumer?

Mr. **Cromwell**. We do not want to make any gifts.

The **Chairman**. What you mean is that we have not supplied the tokens to maintain proper distribution, is it not?

Mr. **Cromwell**. Mr. Chairman, what I mean is that we have never recognized the theory that as the production of the Nation increased due to the saving process within the Nation, it is absolutely essential that the Nation have a central agency appointed to see to it that the flow of money is increased when these finished consumer goods are placed on the market.

The **Chairman**. Absolutely, and if it is any comfort to you, I will say that I am in full accord with that view. I think I know of an illustration that rather covers the situation. My father was always devoted to the care of his horses, and he tried to teach me that when I was a boy, and when he would send a horse to the horse shoer to put on new shoes, he would always say:

> Now, please work on the shoe and adjust it to fit this horse's foot; don't cut off the horse's foot to work it in the shoe.

What you mean is that the tokens should be supplied with proper relation to production, so as to accomplish satisfactory distribution of the goods essential to human comfort and happiness?

Mr. **Cromwell**. Yes; Mr. Chairman. There is no reason in the world to assume that when we have production of goods, such as took place in 1929, that people suddenly do not want goods. That is ridiculous.

The **Chairman**. As a matter of fact, they wanted them and they needed them.

Mr. **Cromwell**. They needed them badly.

Mr. **Fish**. I think Mr. Gifford's question was perfectly correct, and what he wanted to find out is simply this, if Mr. Cromwell was not advocating a system to promote production to the maximum. In other words, it is an economy of abundance, as opposed to the present economy of scarcity practiced by the administration.

It is a perfectly proper question, and it is not necessary that it should be answered, but I concur in it.

Mr. **Transue**. May I ask a question?

The New York Times on Sunday gave a list and showed according to the newspaper comment that corporation profits were greater last year than they have been for a number of years. If your theory is true, why then is there so much unemployment when the corporations are making those profits?

Mr. **Cromwell**. Well, of course, Mr. Transue, some economists claim that the undistributed-profits tax was one cause for the depression, because although these corporations did earn much more than they had earned in several years previously, these taxes were so high that that money was withdrawn and converted by the Government into current expenditures, money which should have been used to further expand plant production and employ more labor.

Now, Mr. Alexander Sachs is one economist who believes that that tax was in a measure responsible for the depression.

Mr. **Transue**. But your statement here is that if corporations do not earn a profit, labor cannot be employed. We have the example here that they have made a profit. Is it that, or is it the fact that, for instance, the automobile factories have no purchasers for their automobiles that is the reason for unemployment, and not the fact that the corporations discontinue to make a profit?

Mr. **Cromwell**. Of course, when they cannot get purchasers, they cease to make a profit.

Mr. **Transue**. Only temporarily. The corporation can wait for the market.

Mr. **Czerwonky**. May I take that question?

Mr. **Transue**. But when the buyers of automobiles cease to buy, the man working in the automobile factory is out of a job and he has not the reserves to carry him over that the corporation has.

Mr. **Czerwonky**. I would like to answer that question.

Mr. **Gifford**. I want to make one more statement. What we want to know is, how will you pump these tokens into the hands of the people that the banks will not lend money to?

Mr. **Cromwell**. I think that the method that we will present tomorrow will include a means to induce the banks to loan money to borrowers.

Mr. **Gifford**. In other words, is it that you must pump that money to them by means of this discount of 15 percent?

Mr. **Cromwell**. No, sir; that has nothing to do with it.

Mr. **Gifford**. You do not approve of this bill?

Mr. **Cromwell**. I approve of the objectives, but I think that Mr. Goldsborough's methods may be improved.

Mr. **Gifford**. I approve of all the objectives of the New Deal, but damn the methods.

Mr. **Cromwell**. If you will wait until tomorrow, I think that I can answer your question.

Mr. **Gifford**. I will be glad to.

Mr. **Czerwonky**. The question you raised was this: Supposing that the corporations made a profit, as you say quite a good-sized profit, and that in the face of declining employment. The statements which are sent out by these different institutions of course do not necessarily indicate profitableness at this quarter of the year. In other words, the statements by corporations indicate the profits for the whole year. Your statistics can be extremely deceiving.

As Mr. Knutson stated before Senator Byrnes' committee, industry—and that means General Motors—produces cars to order, and if they cannot get a profit on the cars, to pay them for certain fixed charges, wages, salaries, and amortization, they automatically curtail operations. We have that condition—administrative control, it is called. It is not monopoly control, and we have that condition in the establishment of prices in the industrial system. We cannot get away from that, for this reason, that these manufacturers—and I am speaking of some of these big men in charge of the corporations—are acting as trustees for a group of stockholders, and their primary responsibility is to earn profits.

Mr. **Transue**. I want to ask a question right there. Why should a farmer, then, grow a bushel of wheat when he cannot sell it? Why should he not have the same privilege that the automobile manufacturer demands before he will turn a wheel?

Mr. **Czerwonky**. I would like to answer that question. I have a prepared statement on that.

The **Chairman**. I think the committee will have to adjourn. This is all very interesting, but the members wish to be on the floor of the House.

Mr. **Transue**. I would like to have an answer to that question.

Mr. **Czerwonky**. I will gladly answer it for you tomorrow.

Mr. **Transue**. Very well.

The **Chairman**. Very well, gentlemen; the committee will recess until 10:30 o'clock tomorrow morning.

(Thereupon, at 12:15 p. m., an adjournment was taken until Thursday morning, February 10, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, FEBRUARY 10, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on H. R. 7188 were resumed at 10:45 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Evans, Mr. Transue, Mr. McGranery, Mr. Barry, Mr. Wolcott, Mr. Fish, Mr. Gifford, Mr. Luce, and Mr. Crawford.

The **Chairman**. The committee will come to order.

Mr. Cromwell, you may resume your statement.

STATEMENTS OF JAMES H. R. CROMWELL AND HUGO E. CZERWONKY

Mr. **Cromwell**. Mr. Chairman, might I ask the forbearance of the committee again, and request that I be allowed to complete the second part of my statement without any interruption, if possible.

The **Chairman**. Proceed. We shall be glad to hear you.

Mr. **Cromwell**. Thank you, sir.

In my appearance before this committee yesterday I explained the working of our modern capitalistic system, and emphasized the necessity of synchronizing the flow of dollars with the flow of finished consumer goods if we are to put an end to intermittent production and the widespread human suffering which the latter entails.

Today it is my purpose to discuss briefly practical and positive means of attaining and maintaining synchronization. Mr. Goldsborough's bill, H. R. 7188, is one method of attaining the goal. It provides a positive mechanism for controlling the flow of dollars, and for maintaining profitable conditions for business as a whole. However, we believe this bill presents a very difficult problem from an administrative point of view. In our opinion the same objectives outlined in the preamble of the bill can be attained without encountering the following administrative difficulties:

(1) The necessity of licensing all retailers, property owners who rent homes, hospitals, private schools, theaters, et cetera, and the necessity of policing these millions of bodies to prevent fraud. Considerable governmental expense is inevitable.

(2) The necessity of vast amount of additional clerical work by retailers in making out sales vouchers, interfering with efficiency in

retailing. Under modern conditions there are generally no records of physical sales excepting through checking inventories at stipulated times, most sales being on the books and sometimes on a slip given to the customer.

(3) The necessity of handling an immense quantity of retail sales vouchers by banking institutions, the cost of which would, in the long run, have to be paid by the customers, or consumers.

(4) The necessity of having to provide another source of revenue for the banks probably by levying service charges on check writing. The banks must be compensated for their bookkeeping and check-clearing services as the volume of check writing increases in order to maintain them in a healthy financial condition.

(5) The necessity of establishing another monetary agency such as the National Credit Commission to supplement the Federal Reserve Board.

We are particularly alarmed over the extensive licensing power which is placed in the hands of the Secretary of the Treasury. Abuses might well arise in this personal relationship between Government employees and private citizens.

We also believe it to be highly essential to reverse the present role of the commercial banker from that of being primarily a purchaser of bonds to that of being a merchant of credit. This would make available intermediate investment funds to small independent producers on the same terms as such funds are available to large corporations. Only in this manner can we hope to maintain competitive conditions in industry without which monetary control cannot be effective. H. R. 7188 would not reverse the existing trend of investment in our banking system from bonds to loans to businessmen.

We believe the simplest possible administrative mechanism should be introduced, and with this thought in mind propose that the Federal Reserve Board be equipped with the following three methods of making dollar additions:

1. To empower the Board to originate dollar additions and make grants to the Treasury.
2. To empower the Board to permit commercial banks to originate dollar additions, if deemed desirable, by lowering reserve requirements.
3. The empower the Board to induce dollar additions by subsidizing bank loans to private enterprise.

The first and third methods represent positive means of making dollar additions and they would be used to supplement the second method in case the latter failed to function as desired and required. The Board, in other words, would normally use the second method to augment our flow of money; that is, it would lower reserve requirements. While the third method is primarily an emergency measure, designed to rout the widespread unemployment and underproduction which exist today, in the event of a national emergency all three methods might be used simultaneously.

The direct creation of dollar additions by the Board and their allocation to the Treasury in the form of grants, should be provided for by amending the Federal Reserve Act as follows:

A. The Board may, from time to time, credit the account of the Secretary of the Treasury with such sums in the form of grants as in its discretion may be necessary to maintain synchronization. Said sums shall promptly be expended by the Secretary of the Treasury in accordance with such recommendations as shall have been previously suggested by the Board and approved by Congress.

Now, so far as these grants to the Treasury are concerned, there are three major purposes for which the new dollars could be used and which would directly affect the functioning of our economy. They are as follows:

(1) Use of the new dollars to pay part of ordinary governmental expenses.

(2) Use of the new dollars for public works or work-relief projects or to meet old-age benefit payments.

(3) Use of the new dollars to redeem part of the national debt.

Should grants to the Treasury be used to pay part of ordinary governmental expenditures, that is, should grants be used to reduce taxes, the dollars would positively augment the national flow of money and proportionately raise the purchasing power of the community. In this case the new dollars would actually be put into circulation by the recipients of checks from the Treasury issued in payment of current expenses. No administrative problem would be involved, i. e., no licensing or policing.

In the event that public works projects were inaugurated the new dollars would be put into circulation by the various contractors who would be paid with Treasury checks as construction progressed. Suffice it to say at this point, however, that we do not consider public works projects comparable in efficiency to tax reductions because tax reductions would be immediate and positive in effect, whereas the flow of new dollars allocated to public works projects would be dependent upon the progress of construction. It is, of course, needless to say that old-age benefit payments would, like tax reductions, be immediate and positive in effect.

Were the new dollars used for debt redemption they would be available for investment in private enterprise by the former Federal bondholders. If these funds were promptly reinvested the new dollars would be put into circulation by the expenditures of private enterprise.

Since grants by the Board to the Treasury would eventually be credited to reserve accounts of member banks, such banks, under present regulations, could multiply these new reserves anywhere from one to five times by expanding their loans and, in consequence, the purpose of origination by the Board would be frustrated. Such unregulated creations of dollars by the banks must positively be prevented by amending the Federal Reserve Act to equip the Board with the power to control reserve requirements. It needs to be clearly understood, of course, that the primary function of reserves is to control the volume of demand deposits or check money. The amendments should be as follows:

B. The Board, upon the affirmative vote of not less than four of its members—in order to prevent injurious credit expansion or contraction, to regulate the value of money, to promote increased administrative efficiency and to assure a fair and just return to member banks and their stockholders—may, by regulation, change the requirements as to reserves to be maintained against demand or time deposits or both, by all member or nonmember banks.

C. The legal reserves of all member or nonmember banks shall be on deposit with the Federal Reserve bank of their respective districts.

It is important to understand clearly that the raising of reserve requirements to offset dollar additions made by the Board would not decrease the earnings of our banks or injure them in any way because the earning assets of the banks would not be diminished. Moreover, complete flexibility would be assured, since the Board could permit the banks themselves to make the required dollar additions by expanding private loans, if this was necessary to maintain our banking system on a profitable basis. Similarly, if an outflow of gold should contract deposits and deplete bank reserves the Board could at once offset such a threat to the national flow of money and to bank profits by reducing reserve requirements. Conversely, if an inflow of gold engendered an undesirable expansion of deposits and reserves, which took place last February, the Board could proportionately raise reserve requirements. But let me explain in more detail the vital importance of empowering the Board to regulate these factors.

No medium of exchange even begins to approach the safety, efficiency, and convenience of check money and the service which our banks render to the Nation, not only in clearing checks but in loaning and safeguarding the funds of depositors, is of vital importance to the functioning of modern capitalism. For these reasons it is essential that our banks be assured a fair return on their invested capital.

When, therefore, it was the opinion of the Board that the earnings of our banks ought to be increased, it could originate new money and permit the banks to make dollar additions on the basis of the new reserves so created by not proportionately raising reserve requirements. Or, on the other hand, if the Board desired to bring about additions in dollar flow without itself originating any new money whatever, it could simply reduce reserve requirements, thereby permitting the banks to create new money without impairing their reserves.

This, of course, is the second method of increasing our national flow of dollars with which we suggest the Board be equipped. It is obvious, however, that this second method alone, would be just as ineffectual and futile as open-market operations are today. But if the Board were authorized to make grants to the Treasury, we are convinced that the power to lower reserve requirements would become an effective instrument of monetary control.

It would become effective because member banks would be faced with two alternatives. They would either have to avail themselves of the privilege of increasing their income-earning assets by making new loans, that is to say, by increasing their deposit liabilities, or their deposit liabilities would automatically be increased without their gaining any profit, as the result of grants to the Treasury.

Faced with such an alternative, which, let me repeat, does not exist today, it seems safe to assume that our banks would be persuaded to grant loans to business on mutually satisfactory terms.

And now let us examine the third method of making dollar additions, which would empower the Board to induce enterprisers to borrow and bankers to lend. It provides a means whereby loans up to 10 years' duration can safely be extended by bankers to businessmen on a basis which would convince both parties that there would be an opportunity to make a profit. It proposes, in short, to authorize the Board to subsidize enterprisers to use money and to pay banks a profit or service charge, for the risk and expense involved in extending loans to such enterprisers as will increase production and employment. It would especially apply to small-business men whose justifiable demands for more and easier credit were unanimous at their recent meeting at the Department of Commerce. The idea of subsidizing producers and our banks at the expense of taxpayers might, at first glance, appear unjust, expensive, and impracticable, but this is not so for numerous reasons. Before discussing these matters, however, let me first set forth the precise powers which Congress should authorize the Board to employ in order to initiate inducement loans:

1. The Board, or its duly appointed agents, is hereby authorized to certify such loans extended to borrowers by banks of deposit as hereafter shall be designated as "inducement loans for increasing commercial production."

2. "Inducement loans for increasing commercial production" refer to extensions of credit granted by member banks to increase the flow of industrial and agricultural products and to increase the fixed inventory of distributors and specifically excludes loans for consumption, refunding, or speculation. Such loans shall be amortized within a period of 10 years from date of extension and shall be repaid in annual installments in accordance with such regulations as may be promulgated by the Board.

3. The rate of interest on inducement loans shall be established from time to time by the Board and may be positive or negative as conditions require. The certification of such loans is intended to protect the Board in the disbursement of inducement subsidies to borrowers and in the granting of service charges to member banks when necessary.

4. The Board may credit the accounts of member banks with such inducement charges as it may authorize such banks to credit to borrowers whose applications have been certified to be eligible as inducement loans and may further credit member banks with such service charges or interest rates as in its discretion will not only reimburse said member banks for the expense and risk incurred in extending inducement loans to borrowers but will encourage them to extend such loans.

These provisions grant the Board full jurisdiction over the rate of subsidies both to the banks and to enterprisers to the end that any unjustified contraction in our national flow of money could promptly and positively be offset. Such rates would, of course, apply to banks and enterprises as a group and not individually. The minimum service charge which would be granted to banks would probably be 3 percent; that is, the average income they would receive from Federal bonds, but these charges could be increased to whatever extent was deemed reasonable to induce the banks to grant loans.

Subsidies to enterprisers would vary according to the state of mind of the business community; they might be only one or two points below the prevailing interest rates or, in the event of an emergency like this or the 1929 depression, negative rates could be authorized whereby enterprisers would not only pay no interest but would be paid 6 percent or more to take a loan that would result in the employment of labor.

The certification of inducement loans by the Board would be for bookkeeping reasons and to make certain that the loans extended were used only for purposes which would at once increase production and employment. As soon as dollar additions were made to flow by the banks the Board would, of course, begin to reduce the rates on subsidies until normal bank-interest rates were again established. Let us now see an example of the method of operation, and the costs involved, in the extension of an inducement loan.

In this example, $1,000 is loaned to an enterpriser for a period of 10 years and requires repayment in yearly installments of $90 each. The Board could permit enterprisers as a group to make smaller repayments during the first few years and correspondingly increase their installments later on. Enterprisers might find it difficult to meet first or second installments out of earnings, but probably could pay later and heavier installments with comparative ease. The interest rate is minus 3 percent, and the service charge granted to the loaning bank by the Board is computed at 3 percent.

On the next page, gentlemen, you will find an inducement loan in detail, as an example.

(The example referred to is reproduced below.)

Amount of loan	**$1,000**
Length of term (in years)	**10**
Rate of interest (percent)	**—3**
Yearly installments (each)	**$90**

Annual periods	Yearly installments	Interest, −3 percent	Total paid on principal	Amount of principal still unpaid	Service charge of member bank [1]
1	$90.00	−$30.00	$120.00	$880.00	$30.00
2	90.00	−26.40	116.40	763.60	26.40
3	90.00	−22.91	112.91	650.69	22.91
4	90.00	−19.52	109.52	541.17	19.52
5	90.00	−16.24	106.24	434.93	16.24
6	90.00	−13.05	103.05	331.88	13.05
7	90.00	−9.96	99.96	231.92	9.96
8	90.00	−6.96	96.96	134.96	6.96
9	90.00	−4.05	94.05	40.91	4.05
10	39.68	−1.23	40.91		1.23
Total	849.68	150.32	1,000.00		150.32

[1] Computed at 3 percent. Rate to be established.

Bookkeeping entries for inducement loans and service charges on such loans

BOOKS OF LENDING BANK

Debit:		
Notes receivable:		
Note given by enterpriser	**$849.68**	
Note given by the Board	**300.64**	
Credit:		
Enterpriser		**$1,000.00**
Service account		**150.32**
	1,150.32	**1,150.32**

BOOKS OF THE BOARD

Debit: Business stability account	**$300.64**	
Credit: District Federal Reserve bank		**$300.64**

Mr. **Cromwell.** We see from this example that the total invisible cost to taxpayers over a 10-year period of inducing the flow of $1,000 would be $300.64. We call the costs of inducement loans "invisible" because they are, as shown by the example, simply credit entries on the books of the Board. Since these credits would ultimately be deducted from grants which otherwise would be made by the Board to the Treasury, taxpayers would never be directly assessed to pay any part of the costs of inducement loans.

The chief virtue of inducement loans is that they are designed to obey the demands of human instincts instead of compelling human instincts to obey the demands of arbitrary regulations. They would not compel but would induce cooperation between borrower and lender by injecting into every transaction the practical human factor of self-interest or profit. Once enterprisers were induced to borrow money they would employ labor to increase their production or to add to their productive facilities; the higher consumption of these formerly unemployed workers would increase the demand for more production, and thus the productive-consumptive process would be stimulated to capacity and our unemployed would be taken up by private industry.

The inducement to an enterpriser to use this new money, and thereby to employ labor and increase the flow of consumer goods; would be very great. The enterpriser and his investors would have the use of $1,000 for 10 years without interest; and when the last installment had been met a total of only $849.68, instead of $1,000, would have been repaid.

The fact that the Board could go to a far greater extent in subsidizing enterprisers, if such action was necessary, should be fully appreciated. Negative interest subsidies could be raised to 6 percent or more and the opportunity for profit made so attractive and lucrative to enterprisers that additional business activity and increased employment positively would take place.

The inducement to the banks would also be very great. The occasions when inducement loans would be authorized by the Board would generally be during "hard times" when banks would fear to create additional liabilities by granting new loans. It is during just such periods of depression, i. e., when banks are unwilling to grant new loans or to loan out the savings of their depositors at normal interest rates, that enterprisers require long-term loans at low or negative interest rates. The last 7 years are a good example of what is meant and the demands for credit of the little business conference last week clearly demonstrate that this condition is extremely acute at this very moment. With inducement loans, however, the banker not only would receive a profit for accepting the risk at a time when overhead would probably have become a serious problem, but he would be privileged to create new money on a long-term basis and would be protected in the event that depositors demanded currency during an emergency or for seasonal requirements.

It must, of course, be distinctly understood that the banks and not the Board would be extending the loans and assuming all risks involved. In this respect inducement loans, in addition to the other liberalizing provisions we are suggesting, would represent a return to the old precepts of personal banking, now a rapidly vanishing factor, the restoration of which we believe would greatly benefit the Nation.

The absence of the element of personal trust and confidence in granting loans, and the substitution of strict adherence to arbitrary regulations requiring collateral, and so forth, which are rigidly enforced by bank examiners, have forced many thoroughly reliable and honest borrowers into the hands of loan sharks. Such a condition of affairs is both retrogressive and wholly unwarranted, and should be immediately corrected. The only requirement demanded by the Board, so far as inducement loans are concerned, would be that of productivity. Provided, therefore, that banks could prove to the Board or its agencies that their loans would be used for productive purposes, all other elements involved in the risk would rest solely upon the judgment of bank executives.

It should likewise be understood that certification by the Board would not only guarantee the payment of service charges but would also guarantee the eligibility of inducement loan paper for cash advances in case of an emergency. The risks assumed by banks which granted inducement loans would, as a result, be minimized by two important elements, i. e., first, the ability to obtain currency in the event that depositors demanded it; and second, the fact that the installments of borrowers would be reduced by subsidies and the length of time allowed should assure the ability to pay and thereby increase the factor of safety.

The advantage to the taxpayers, i. e., the Government, would even surpass those enjoyed by the enterpriser and the banker.

First, the Nation would benefit by the increased business and employment which would result from the ability of the Board to close the gap between lenders and borrowers.

Second, the Nation would be spared the corruption inevitable if politicians replaced our highly-trained bank executives as lenders of money, as is now being proposed for the R. F. C.

Mr. **Gifford**. You mean the Federal Reserve Board?

Mr. **Cromwell**. No, sir.

The **Chairman**. You were speaking of replacing the service now being rendered by the R. F. C. That is what you mean?

Mr. **Cromwell**. Yes, sir.

Mr. **Gifford**. I thought you meant the taking over by the Government of the Federal Reserve banks.

Mr. **Cromwell**. No, sir.

Mr. **Gifford**. Your remarks would apply to that, would they not?

Mr. **Transue**. Can you give us a bill of particulars which you are speaking of there about corruption?

Mr. **Cromwell**. I will as soon as I finish, Mr. Transue, if I may.

Third, the Nation would be relieved of taxes for doles, public-works projects, and other forms of relief, because unemployment would be taken up by the increase of production in private industry.

Fourth, by granting to the Board the power to create economic conditions which would stimulate business activity, full utilization of our productive capacity and general prosperity should rapidly be achieved. The loss in income to the Nation from 1930 to 1934, resulting from the wasted productive capacity of our idle factories and millions of unemployed workers, has been calculated to total at least 180 billion dollars. That comes from the Brookings Institution, Income and Economic Progress, 1935, page 22, and it is important to realize that these losses are, at the present moment, averaging about 100 million dollars per day.

Now, while our proposed amendments would permit the Board to neutralize the effect of gold movements, either by raising or lowering reserve requirements, the gold cover clause of the existing Federal Reserve Act could compel the suspension of such a policy and could thereby precipitate a national disaster.

The gold cover clause in the existing act requires that Federal Reserve banks must maintain a reserve in gold of not less than 40 percent against their paper dollars in actual circulation, and a reserve in gold of not less than 35 percent against their deposit liabilities or credits to the accounts of member banks. In the event, then, that foreign demands engendered an outflow of gold, and if adherence to synchronization simultaneously required an expansion of check money, the Board might be compelled, by the insufficiency of gold reserves, to sacrifice the policy of synchronization in order to maintain minimum gold reserves. In other words, if an increased flow of finished consumer goods required the augmentation of our dollar flow, and if the insufficiency of gold reserves forbade the Board to make further dollar additions, synchronization would have to be abandoned.

It is obvious that our dollar flow cannot simultaneously be synchronized with finished consumer-goods flow and with an arbitrary quantity of gold reserves; therefore the domestic relationship between check money, currency, and gold reserves which now exists by statute must be definitely severed. To accomplish this purpose, we suggest still another amendment to the Federal Reserve Act, which is as follows:

> **Section 16, paragraph 3, governing gold cover for note issues and deposits, is hereby repealed in its entirety.**

It is our belief that the measures herein suggested would provide the Board with ample power to safeguard our economy against any manipulations or movements of gold which could possibly occur.

I wish to emphasize that the inauguration of the new administrative machinery provided by our suggestions would, in no way, alter or upset either our economy or our present banking system, nor would any loss thereby accrue to our banks and their depositors and stockholders. No changes would have to be made in our fractional reserve banking system since the only modification involved would apply to the powers of the Board itself; no physical difficulties, therefore, would be encountered in the transition to what I term a scientific money system. In short, such a transition would benefit our banks and the entire Nation, because the new system would permit positive control over dollar flow and would guarantee the restoration and maintenance of business stability.

Equipping the Board with a positive "brake" is represented by our proposed amendments to the Federal Reserve Act which provide for the raising of reserve requirements; this is, of course, in addition to control through the rediscount rate and through the tradition against interbank borrowing. These increases would, of course, take place gradually and without friction. Bank earnings would not be reduced because increases in the reserve ratio would be ordered only to prevent multiple expansion of additions to the dollar flow and outstanding earning assets would therefore not be diminished in any way.

Equipping the Board with a positive "accelerator" is represented by the powers which provide for making additions to the dollar flow by inducement loans and grants to the Treasury. Under normal conditions the authority to reduce reserve requirements, supplemented by the power to make grants, should suffice to maintain synchronization and assure full capacity production while under abnormal conditions, such as have existed since 1929, a more powerful and direct "accelerator" is provided by the introduction of inducement loans. This positive method of injecting new money directly into productive enterprise might be more aptly compared to our modern "supercharges" rather than to an "accelerator."

In conclusion, gentlemen, may I call your attention to the fact that while it seems safe to assume the powers we suggest be granted to the Board by Congress would equip it with the "brakes and accelerators" necessary to achieve synchronization, and thereby to control and stabilize our economy, there is involved no coercion, no imposition of planned production, no buying or taxing submission from private business. In short, private business would suffer no interference.

A coercive control has no place in a democracy. What is herein proposed involves no bureaucratic regimentation or anything remotely approaching it, and there is no delegation of power to a central authority which would compel individuals to do what that authority thought was best for them. The capitalistic ideal of free enterprise could function smoothly and with safety, and individuals could pursue any line of endeavor their ambition, tastes, or capacity might cause them to prefer; there would be no interference with the free selection of goods by the people nor with their right to save, hoard, invest, or consume as they might desire. The purpose of the positive monetary mechanism herein set forth is to safeguard the individual, his property, and his right to earn a living, and the inauguration of such a mechanism would not involve the sacrifice of one iota of the political freedom now guaranteed to American citizens by the Constitution.

Now, Mr. Chairman, if I might ask the forbearance of the committee for about 5 minutes more, I have received a letter from Prof. Edwin R. A. Seligman, who I think most of the members will agree, is one of the foremost economists in the world, and one of the most respected economists in the world.

At the time these inducement loans, or what was popularly known as the negative interest, was first introduced to the public at the hearings of the Senate Agricultural Committee last summer, there was a great deal of ridicule and criticism directed toward these suggestions, so that it is with some gratification that I should like to be allowed to read to the committee the statement which Professor Seligman has authorized me to make to the press and to the committee, in which that proposal of inducement loans is given favorable mention.

May I have your consent to read that letter, Mr. Chairman, from Professor Seligman?

The CHAIRMAN. I am wondering when the committee will have an opportunity to interrogate you.

Mr. Cromwell. As soon as this is completed.

The Chairman. All right.

Mr. Cromwell. It is as follows:

Suggestions for Meeting the Present Business Recession

(By Edwin R. A. Seligman, professor emeritus in residence, Columbia University)

The interesting suggestion as to "inducement loans" made by my friend, James Cromwell, in his recent book, seems to me well worthy of careful consideration. It rests upon two ideas. One is that in times of actual or impending business depression the Government is in last resort justified in stepping down as a result of the producer's inability to see a chance of profit, owing to an inadequate margin of sales price over costs. This inadequacy may be due either to excessive costs or to insufficient price as a result of lower consumption.

Hitherto banks have come to the rescue by reducing interest rates, and Government has tried to help by increasing outlay or consumption. Mr. Cromwell's suggestion is that it would be appropriate for the Government to come still further to the rescue by reducing producers' costs through the lowering of interest to a negligible figure, going even so far as the point of minus interest, i. e., by granting a subsidy rather than making a charge, in order to increase the producer's margin of price over cost.

It is realized that the carrying out of this suggestion would involve great difficulties in determining the character and choice of the enterprises to be helped. It would, in my opinion, be far preferable if private industry would itself undertake this task, with the assurance of help from the Government, if needed. It is also realized that at present any such private activity would run up against our well-intended but foolish antitrust law.

I am convinced, however, that sooner or later some such cooperative activity will become necessary. Just as our banking structure was immeasurably improved when, through the adoption of Paul Warburg's suggestion, united reserves took the place of the previous independent or individual system, so the anarchy of our present industrial system, which leads to the disastrous periodic swings in industrial life, can be effectively overcome only when the necessary incentive of private profits is combined with some cooperative activities in investment and production. For this incentive of private profit must be preserved at all costs as against the foolhardy but seductive ideas of socialism or communism. This cooperation, however, demands the greatest wisdom and must be based on much experience. It ought to be accomplished by private effort, seconded ultimately by Government advice and possible assistance. That assistance may take the form, in part, of "inducement loans."

We are only on the threshold of understanding the causes of business depressions. When the combination of economic research and business experience brings us to this better understanding, the suggestion of "inducement loans" may well play a part in the preventive or remedial program. What is needed at present, above all, is a joint effort of business and Government to grasp the problem and to be permitted to work hand in hand in solving it. Neither the business demand for "hands off" nor the Government opposition to the "malefactors of wealth" will avail. The one spells anarchy, the other regimentation. Only by a judicious and conservative cooperation can the problem ever be solved.

The Chairman. Mr. Cromwell, have you in mind any plan of currency or credit supply that would work automatically?

Mr. Cromwell. I will let Mr. Czerwonky answer that, if I may rest my throat a few minutes.

Mr. Czerwonky. It is my belief that there has to be some authority provided in order to control the credit supply or the flow of dollars, as we term it. In case this mechanism of inducement loans is not instituted, in our belief the power of the Board to make grants to the Treasury, plus the power to control reserve requirements, represents the simplest mechanism which the Board could possibly have.

The **Chairman**. You do not believe that we can have an automatic system?

Mr. **Czerwonky**. No, sir.

The **Chairman**. You do not think that the use of the available credits that we have been accustomed to using as money would supply that kind of a basis?

Mr. **Czerwonky**. No, sir. The present controls, as they exist in the reserve system today, control over reserve requirements, open-market operations, and the rediscount rate, and, of those, I believe the members of the committee realize that the open-market operations is the most effective, all of these three controls only work positively in one direction; that is, they are only positive in placing restrictions upon excessive additions in the amount of demand deposits or in the flow of money. They are not effective in going in the other direction, i. e., in bringing about additions in dollar flow. As Mr. Goldsborough indicated the other day through an example, we can take a string and tie it onto this table, and we can pull the string and the table toward us, but we cannot push on a string, and that is the position the Board of Governors is in today.

The **Chairman**. Do you mean to say that the Board of Governors of the Federal Reserve Board has exhausted its power in doing the positive service to which you refer? Have they directed their efforts in that way?

Mr. **Czerwonky**. Whether they have directed their efforts in that way or not, the point is, Mr. Steagall, that the member banks have approximately $1,390,000,000 of excess reserves, and the reserves are not being employed. If they resorted to additional open-market operations, all that would happen, probably, would be an increase in the excess reserves available to the member banks and present bondholders would come into possession of idle funds.

The **Chairman**. If it would not affect the situation, why is it that those who are opposed express such great fear that it would have the very result that you say it woud not have? Your contention about that seems to me to be rather new.

Mr. **Czerwonky**. Would you state that again?

The **Chairman**. I say, if it would not have that effect, to add to your supply of currency, why is it that those who are opposed to it have such fear that it would do that?

Mr. **Czerwonky**. Well, I believe that the only fear that might exist in the minds of some of these men is this: The fact that at some future time the excess reserves which are made available through the open-market operations may be utilized, and they provide a base——

The **Chairman**. They would have the power to reverse their policy, but you say that the reversed policy is very easy to exercise?

Mr. **Czerwonky**. That is right.

The **Chairman**. That need not disturb anybody.

Mr. **Czerwonky**. The way the Board is set up now, they have utilized fully their power of raising reserve requirements. The thing which is important——

The **Chairman**. But they have not used their powers in the reverse direction to the limit, by any means.

Mr. **Czerwonky**. I think the thing which is exceedingly important is this thought, that the essential thing is to get dollars into the hands of the ultimate consumer. Open-market operations only place the dollars in the hands of investors, and these investors in turn must find a place for the use of them. If the business community does not care to use the dollars, then the system becomes stagnant.

The **Chairman**. Do you hold the view that the amount of money that you can pile up in the banks does not have any tendency toward their releasing their dollars, or toward the enlargement of the activities of the banks in supporting trade and commerce?

Mr. **Czerwonky**. The making available of additional excess reserves I do not believe would be very satisfactory, for this reason: That manufacturers as a group have desired increasingly since 1920 to acquire investment funds on a basis which would give them independence. Now, the only way that they can get investment funds which will provide for independence is through an arrangement whereby the funds are gradually amortized out of earnings. There is a tradition within the banking system—and I am speaking of the commercial banks—to extend loans only over periods of 30, 60, and 90 days, or 2 years at the utmost, and that tradition, in our belief, has to disappear before the instrument of open-market operations will really become effective. Businessmen as a whole will otherwise not desire to use bank funds. They will prefer to float a bond or stock issue. We believe that without placing the power in the Board of Governors to make grants to the Treasury, there is not any means for bringing about the use of the excess reserves which are made available through open-market operations. In other words, the banks have these alternatives upon the adoption of the proposed amendments, and which Mr. Cromwell indicated in his statement. We will give them, first, the opportunity through the lowering of the reserve requirements, if they are short in reserves, to increase their loans and investments. If they do that, they will increase their earning assets and will, of course, simultaneously increase their deposit liabilities to the community as a whole. That is good business as far as the commercial bankers are concerned. It means profits as far as the stockholders of these institutions are concerned. If they do not avail themselves of that privilege, of increasing their loans and investments, then the power of making grants to the Treasury will place them in a position where they will increase their deposit liabilities to the community, but not increase their income-earning assets.

We believe that in the presence of these alternatives, of increasing their deposit liabilities and their earning assets, or increasing their deposit liabilities and not increasing their earning assets, the banks will promptly put to work the excess reserves which are made available through control over the reserve requirements.

We are suggesting that open-market operations be virtually abandoned and for this reason, that when open-market operations are instituted, the Board of Governors has practically no control over how the excess reserves are employed. If the member banks' reserves are reduced through the actions of the Board, under those conditions, then, making an outright gift to these member banks, it is perfectly reasonable for the Board to ask or demand that these funds be used for nonspeculative purposes.

That is one of the reasons why——

The **Chairman**. After all, you do not think that we need any additional machinery to deal with the difficulties that confront us now?

Mr. **Czerwonky**. We do not require any new body, we will say, as suggested by Mr. Goldsborough, a commission. All that we require, in our belief——

The **Chairman**. You want to use the present organization and system as set up now?

Mr. **Czerwonky**. That is right.

The **Chairman**. And, when you got through, if we did all of the things that you are talking about, the controls would be in an administrative body such as the Federal Reserve Board, with its open-market committee, and their set-up?

Mr. **Czerwonky**. That is right. The open-market committee, though——

The **Chairman**. And when the Board failed to do the necessary thing to get the necessary results, we would be where we are now.

Mr. **Czerwonky**. Then it would be entirely up to the members of this committee to demand an explanation, but I do not think it is fair to accuse a body which is assigned a task and has not the instruments to carry out the task—I do not believe——

The **Chairman**. You do not believe that the powers that now exist in the Federal Reserve Board are sufficient?

Mr. **Czerwonky**. That is right. I believe that we only have a one-way mechanism in the Federal Reserve System today. That is true with practically all of the central banks in the world.

The **Chairman**. I would not for a moment offer an opinion in contravention of yours, but I do not see where you are right in that. It seems to me that the Federal Reserve Board has all the power that it needs.

Mr. **Gifford**. I well recall that Mr. Eccles said that he could put an automobile in reverse, but that there is no pushing business with a string. But the point that I want to raise is this: Suppose that you gave them the extra power of a negative loan; wouldn't everybody be unwilling to produce anything at all until they got a negative loan? Would you put a man in competition with his neighbor by giving him a negative loan, and making the others follow the usual procedure?

Mr. **Czerwonky**. I anticipated that question, and have a prepared statement on that.

Mr. **Gifford**. Can't you give me anything but a prepared answer? I do not want canned answers. Can't you answer it outright?

Mr. **Czerwonky**. I think that it would be much more satisfactory if I gave you this prepared answer.

The **Chairman**. I want to ask a question along that line. I want to know how you are going to apply your grant system temporarily to a limited number of citizens for a limited period, and then back off from it and resume the other system. We found that it is a little difficult to get away from the emergency remedies that we applied.

Mr. **Czerwonky**. What we are suggesting is in the nature of permanent control within the Federal Reserve System.

The **Chairman**. The machinery is permanent, but its use is only to be resorted to on occasions of accentuated necessity.

Mr. **Czerwonky**. Your question was—and I would like to answer Mr. Gifford's question first——

Mr. **Gifford**. Can't you answer it without referring to that statement?

Mr. **Czerwonky**. I think that this is more satisfactory.

Mr. **Gifford**. To you, probably.

Mr. **Czerwonky**. We have thought this over very carefully, and I think that the question should not be answered offhand. I think that it requires mature thought.

Mr. **Gifford**. I have not anything to base my questions on. I do not see why we need to have this canned stuff here.

Mr. **Czerwonky**. I am entirely willing to take your question on the catch-as-catch-can basis.

Mr. **Gifford**. You ought to answer it immediately, without hesitation.

Mr. **Czerwonky**. Permit me to read this first, and then if there are any questions in your mind, I will answer further.

Mr. **Cromwell**. I suggest that as some of the members of the committee object to the reading, that this be put in the record. We have these answers to questions that, as you say, are canned, and if they may be entered into the record, because that is the purpose that they were prepared for, that will be satisfactory to us, and if Mr. Gifford wants that question answered other than the answer on the paper, that can be done.

(The answer to the question of Mr. Gifford, and previously prepared by Mr. Cromwell and Mr. Czerwonky, is as follows:)

Let us consider the merits of the chief objection to inducement loans, which is likely to be raised. The executives of concerns which were adequately financed might protest that the Board, in authorizing inducement loans, would be supplying their smaller and weaker competitors with capital funds at rates which would permit the latter to operate at lower costs and possibly undersell them. There are three answers to this objection:

First, inducement loans would not be discriminatory and would be available to any enterprise, no matter how adequately it might be financed, which would be willing to increase production and employ more labor.

Second, in the event of a business recession the earnings of all business concerns would be reduced and their existence jeopardized unless positive measures were promptly adopted to prevent any unjustified contraction in the national flow of money. All business and commerce, on the other hand, would benefit by the stability of earnings which would be assured by the maintenance of full employment and capacity production.

Third, the Board, even with its present limited powers, could bring about "easier money" by lowering rediscount rates and inaugurating open-market operations, if it should become evident that a business recession was at hand. Such action, therefore, would tend to lower interest rates for current borrowers in any event. Objections might, of course, be raised to this answer on the ground that these reductions in the cost of money would apply only to short-term loans. The amendments herein recommended, however, do not contemplate any sharp distinction between short-term and long-term loans.

Mr. **Czerwonky**. I think the question was, would not an unfair advantage be granted to present enterprisers who had acquired funds, we will say, through the flotation of a bond issue, and paid a high rate of interest in competing with those who now receive funds through the inducement loan method—is that your question?

Well, as a matter of fact, powers exist now within the Reserve System to declare open-market operations; and the primary purpose, as I understand open-market operations, is to make funds cheap.

Now, of course, the commercial banker has always considered the funds as being only available for short-term purposes. We draw no such distinction in the length of time for the use of funds. Aside from that, open-market operations, if they were properly employed, would automatically place the prospective borrower in a position where he could get funds cheaper than anyone who had acquired funds previous to that; and this is what inducement loans would do.

In addition to that, of course, we have to bear in mind this, that when the inducement loans are made everybody in the community benefits. In other words, we are maintaining business stability in that process, and that means the regularizing of profits for everybody; so even the person who has funds and acquired them at 4, 5, or 6 percent would benefit by being able, as the result of this addition in dollar flow, to deliver to the market place what his plant was capable of producing; and if that injection of dollar flow did not take place we would come to a condition where we would have economic anarchy.

Mr. **Gifford.** I am not asking you about the general result. I am asking you what attitude certain business people would take when they saw their competitors set up on a subsidy like that.

Mr. **Cromwell.** There is nothing to prevent these other people from getting the subsidy.

Mr. **Gifford.** That is my point. Everybody would demand it and get it.

Mr. **Cromwell.** Yes, sir.

The **Chairman.** Let me ask you a question.

Where would my farmer down in Alabama, that I try to represent, come into this picture? You would have a scheme by which, instead of charging 6 and 8 percent, we would pay them that much to obtain the loan and use the money. That would suit my people.

Mr. **Czerwonky.** The purpose of granting this subsidy is twofold, to bring about increased production and increased private employment, and eventually we have to face that problem. Those unemployed and on the relief rolls would be taken into industry and placed in a position where they would produce useful goods, and anyone who can satisfy the commercial banker in his own community that he was a good risk would be eligible if he increased the rate at which he was producing goods. That is the only requirement.

Mr. **Cromwell.** That is the point.

The **Chairman.** My farmer can increase production. I can guarantee that.

Mr. **Cromwell.** The point is that your local farmer has to convince his local banker that he is a good risk.

The **Chairman.** The trouble with my farmers is that they need some consumers.

Mr. **Cromwell.** That is what we are trying to produce.

Mr. **Ford.** Might I make an observation?

The **Chairman.** All right.

Mr. **Ford.** I will take but a minute.

I am thinking of this credit flow, of this money flow, as we used to think of the Colorado River. This money flow comes in a flood sometimes, and dries up later on, exactly like the Colorado River did. There was a time when it ran over, and in certain seasons of the year you could get all of the water you wanted, and, as a matter of fact, it was like the sword of Damocles hanging over the Imperial Valley, for it might be engulfed at any time. Unregulated, that river had just about the same amount of water in it that it has now, but there were times when you had the reverse of that flood situation.

The banks at the present time have an unregulated flood of credit because of their excess reserves. Thousands of businessmen in the country want that money, but the banker does not think that they have quite the proper standing to get it. Therefore they do not get it.

They used to say about the Colorado River that along its course were millions of acres of fertile land which, once watered, would blossom like a rose, and the United States Government has expended about $165,000,000 to build the Boulder Dam. The Colorado River today is as big as the Potomac in normal times, and the farmers along the Colorado River down to the Imperial Valley now get the necessary amount of water to water their land, and they pay a certain amount for it, and ultimately it will repay the Government what it cost to build it.

If we could devise some method of controlling this hog-wild river of credit, so that it would be utilizable in all seasons of the year and under all circumstances, and made available to all men who had the facilities to use it, that would be a good thing, and it seems to me that the objectives of the Goldsborough bill and of you gentlemen are identical. The methods proposed by you are a little bit different. Possibly they have some advantage by reason of the fact that we do not create a new agency. We are simply offering to some extent the operation of the existing agency by one or two amendments to the Federal Reserve Act, and whether or not that is the solution I do not know, but I will say this, that I think it is a suggestion that is thoroughly worthy of careful study, and I hope that this committee will give it that courtesy.

Mr. Luce. The last sentence that Mr. Cromwell spoke confused me, for I had gathered from the sketch of the program that has been given to us that this was a proposal to go beyond the judgment of a banker as to what is prudent and make loans that will add to the present supply of credit.

Now, this point is of the utmost importance at the moment, because we are told that the administration is studying this problem of giving more lending capacity to little business, as it is called.

Some 3 or 4 years ago this committee devoted many hours to the consideration of that problem. We heard a large number of the smaller employers, and we devised what we thought was as prudent a resource as could be devised. We turned it over to the Reconstruction Finance Corporation, and apparently it has not satisfied those who want to borrow, and it would seem as if the most important measure this Congress has to consider will be the forthcoming proposal as to whether a government should go beyond the judgment of experienced and cautious bankers and add its own power for the lending of money.

We have made several experiments in that field already, where this committee has advised Congress in the matter. We gave those powers to the Home Owners' Loan Corporation, to go beyond the judgment of a prudent lender, with the result that today the Government is in possession of between 100,000 and 200,000 pieces of property, where a proposal of this kind to go beyond the judgment of a prudent lender resulted in taking over the foreclosed property.

I could go on and take too long and point out all of the directions in which the Government has gone beyond the experience which has been accumulated since Shylock and the uses of his money were the forerunners of the present methods of lending money, based upon the opinion of mankind today that it is not prudent to lend money to a man whose character, history, and resources indicate that lending to him is not wise.

I thought in listening to you, Mr. Cromwell, that you went in that direction; that you were, by a mechanism which I do not want to consider for the moment—I am getting down to fundamental principles—I thought that you were adding to the various suggestions before us and before the country as to ways to lend money to the rash, those who cannot satisfy a prudent banker that the resources which will recoup the loan are adequate, but your last sentence led me to think that you did not contemplate that.

It strikes me that it may be important for us to know, in considering this very interesting proposal, whether you join those who want the Government to money unwisely, not as bankers, who know more about it than anybody else, for it is their business, their training, their livelihood, and they are the persons most competent in the community to determine whether a borrower is sound or not—I say, I am anxious to know if you join those who want the Government to lend money that the bankers think unwise. I want it very clearly whether you wish to deny their wisdom, just supersede their judgment and grant money where it is unsafe to do it, or whether you want that limitation first, last, and all the time in your proposal, and let me illustrate:

In my town, Waltham, Mass., 5 years ago there were two banking institutions, one a national bank and the other what we call a trust company, a safe bank. The national bank was conducted by men of prudence, whose loans were cautious, who did not loan money where there was no certainty or likelihood of repayment, and that bank is running today; and by great good luck, my own deposit is in that bank, and I thank God that it was in that bank and not in the other. The other bank was run by men who believed in the things that are now being presented to this Congress in bills before us, and those of the administration, as the newspapers intimate, advising us that the prudent, cautious attitude has been harsh, has been selfish, has been too careful, and that we ought to encourage the type of banking that was done by the trust company, which followed the same principles that are recommended to us in all of these proposals, that money be loaned without adequate regard to the capacity of the borrower to repay.

Now, will you let us know here which school of thought you adhere to?

Mr. Cromwell. Mr. Luce, I believe that the school of thought which I belong to takes a middle road between the two ideas that you have expounded, one the idea of rash lending, and the other the idea of possibly too conservative lending. The whole purpose of these amendments to the Federal Reserve Act is to try to do everything we can to encourage loans by the banks. We wish to avoid any Government loaning agency. We do not want to push the banks into making loans which the bankers would consider poor loans. We do believe that under the present Federal Reserve Act and under the various examinations, State and Federal, which our bankers are compelled to undergo, they are restricted by red tape, and it is our purpose to eliminate as much of that red tape as possible, and to make it safe for the banker to grant loans over an extended period of time in safety to his depositors. There is no reason that we can see why there should be an arbitrary rule fixed by the Board which proposes and makes it law that loans extending over 90 days or a year are not good loans. It seems to us that, in the opinion of the banker, if he desires, for instance, in your town of Waltham, to grant a loan to a manufacturer who he knows is sound for a period up to 10 years, and that loan may be paid in equal installments each year, he should be given the privilege of making that loan if he chooses to do so. We do not propose to force him to make any loan, but we do propose to liberalize the regulations and permit bankers to make loans over long periods of time, installment loans, with safety to their depositors, and we hold that that condition does not exist today.

Mr. Luce. You bring before us another fundamental question that has perplexed this committee through the years, and which must be settled sooner or later. Commercial banking was conceived and has been carried out in this country for years in order to accommodate commerce. It was based upon the short-loan purpose, and we developed alongside of it the investment houses, the investment bankers, to make long-time loans. In the years that I have been on this committee, I have seen almost every year further progress being made by permission of law toward consolidating those two functions, the short-term, commercial function, and the long-term investment function——

Mr. Cromwell. Do you mean in the bank itself?

Mr. Luce. I mean in the bank itself. We have tried to safeguard that within the last few years by laws relating to time deposits, forbidding interest being paid on checking accounts, but permitting it on time deposits.

Now, I come from a State that is exceptionally backward, I presume. We have a law in our State on the statute books requiring that a savings bank and a national bank shall not occupy the same quarters. If they are in the same building, there must be a brick wall without any aperture between the two institutions. We go to that extreme, perhaps, because our fingers have been burned. Our experience has shown us the dangers of consolidating investment and commercial banking. We have been trying here in a feeble way in the last 2 or 3 years to accomplish that same purpose.

I want to tell you frankly that any proposal to combine investment and commercial banking will meet as strong opposition as I, for one, can raise. I do not believe it is safe or right or prudent or wise or best for the community to combine those two things.

Do you believe it is best to combine them?

Mr. Czerwonky. I would like to answer that question.

The point that we are stressing here is that we are trying to get the commercial banks out of the function of being purchasers of bonds. In other words, we are trying to get their assets not subject to these periodic fluctuations, like anything which is listed is subjected to. We believe that if commercial bankers are to increase to a considerable degree their dollar lendings to business enterprises they will have to make those loans which will grant independence to the businessmen.

Through the liberalization of the Banking Act of 1935, with the exception of one-half of 1 percent penalty in the discount rates, the member banks were placed in such a position that in case of emergency they were protected against runs. I think the members of the committee will agree with that. With the conditions which have existed up to date, in my opinion, it would have been actually imprudent for the bankers in your community to make long-term loans, but once we have an effective central-bank mechanism, the conditions which have existed up to date would no longer exist. In other words, these slumps which make any type of investment by commercial banks over a period of greater than a year a risky proposition, even if using good judgment by the commercial banker—that risk would not longer exist. The only risk which would exist would be on the type of product which the manufacturer made, but these periodic fluctuations which have made the judgment of all businessmen absolutely valueless for more than 30, 60, or 90 days would no longer exist if we had an effective central-bank mechanism, because we could control the profitableness of business as a whole.

That is essentially what we are trying to accomplish through these amendments—to make it possible for business as a whole to earn profits day in and day out. That thing is physically impossible to do today.

Mr. **Luce**. I can only answer you, sir, by saying that the directors of my national bank are for the most part my personal friends. I know them well. I think that they are capable of conducting a commercial banking business. But I doubt that they have the experience, the training, or judgment to conduct an investment business, and I do not want my $1,000 checking account loaned for 10 years.

Mr. **Czerwonky**. Well, the point is this, that we have a physical problem within our Nation, as Mr. Cromwell pointed out yesterday, of synchronizing the flow of dollars with the flow of finished consumer goods.

Mr. **Luce**. But you are getting away from the fundamental question. You are getting into a question of detail and machinery. I also call your attention to the basic question involved in the tremendous problems that face this committee——

The **Chairman**. Right there it might be well to say that for many years banking institutions were maintained by the States. Those banks were built up out of community spirit, more or less, community pride, and with the support of community and business activity. They made loans on character, along with other factors that entered into the consideration. They supported the business life of those communities. They built this country, and so long as they were allowed to operate in their own way under normal conditions those communities were able to live their own lives and to carry on business activity without resort to all of the many things that they have been asked to do, and some of which we have attempted to make them do here in Washington. Thousands of these banks were swept away due to the vicissitudes of business and of values, and due to these fluctuations to which you have referred, for which they were not responsible and which helped to ruin the country, and many of these banks were destroyed as a result of the policies and the counsel imposed upon them by the larger banking institutions, and in some instances by the influences and actions of governmental authority in Washington.

If we could set up a Government agency that would prevent these fluctuations and stabilize the value of money and of property, so that businessmen would know how to conduct their transactions over a period of 90 days or 3 years or 10 years, these communities could again resume normal lives without having to come here, as is being done, for relief and for assistance such as we are confronted with every day in the proposals that come before the committee.

Mr. **Cromwell.** I would like to call the attention of the members of the committee to the paper that Mr. Weed has just passed to the members, which shows the money supply of the United States from June 30, 1921 to 1934, and I want to call to the attention of the members the fact that I think this paper shows very clearly what the problem is with which we are faced today.

We see by this paper that in 1929 the adjusted demand deposits of all of our banks were $22,744,000,000, and that by 1933 these adjusted demand deposits, which one of the members informed us yesterday—I think it was Mr. Luce—represent 93 percent of our actual money in this Nation—decreased to $15,163,000,000.

Now, until we can find some positive mechanism to prevent contractions of our money flow such as are illustrated by this paper, Mr. Luce's deposit is not going to be safe. I do not care what kind of a bank he puts it in. Nor is our Nation and our democracy going to be safe, because the more this industrial-capitalistic system of ours grows, the more involved and complex it becomes, and the greater these disasters are going to be in the future, unless we can find some way to prevent this contraction of money.

As Mr. Ford pointed out yesterday, this money is nebulous. He said—what was the expression that you used for it?

Mr. **Ford.** Either nebulous or erratic.

Mr. **Cromwell.** It is an erratic money, and we have to find some way to control this credit money. It is not merely a question of turning the printing presses loose in printing currency. We have to make money flow, and by making money flow, I want to make it perfectly clear I mean money flowing between consumer and producer, and that money must go through the bank and be paid out in the form of wages and the goods reclaimed by these wages, so that we have a continued cycle of production and consumption, and the money does not lie idle nor does the credit lie idle in the banks.

That is the problem with which we are faced, and the only method that we know is the method suggested of inducement loans, or by making grants to the Treasury.

Mr. **Ford.** Might I ask you a question right there?

We are in an age where invention and discovery are probably not at their peak, but at a very high point at the present time, and, as to the character of the commodities that the manufacturers are turning out—well, I have thought of the automobile as compared to the buggy. Suppose that a loan had been made to a buggy manufacturer for 5 years before the automobile had become in general use, but that within 10 years the automobile had supplanted the buggy; that loan would be in bad shape, and that would apply at the present time to refrigerators, for the electric and gas refrigerators are coming in and displacing the ordinary ice refrigerators. The same thing occurred when the automobile displaced the bicycle. For instance, every year there is some new gadget that is coming out that displaces some very popular existing gadget, and things like that pop off once in a while, and some of these loans might for that reason be rather dangerous.

However, there is a factor that you are putting in there that would tend to minimize that, and that is the factor of amortization. Now, I issue a bond for $100,000,000, and the bond or bonds that I issue run for 30 years, and while in some cases there are sinking funds and all of that set up to protect that, still that might occur to a big concern. Take the utilities in the United States today, covering the whole country as they do. This might be a farfetched idea, but there are so-called crazy scientists working on a plan to take electricity directly from the air, and if they should be successful in that, that would result in junking our present power plants, our existing generating plants, and then this vast mass of capital lying there in the form of bonds or stocks might be of no account.

We do not know what the airplane will do to the railroad or even to the automobile, so that long-term loans, unless pretty vigorously amortized, would not be good, but you have provided a protective mechanism in there that to a certain extent would take care of that situation.

I want to ask you one question in that connection, however. How would your plan compare in effectiveness with the 100-percent reserve plan talked about? Would you make a contrast on that?

Mr. **Czerwonky**. I have a statement on that which deals with it as it should be dealt with. I do not believe that that question should be answered just in one or two sentences. I think it is absolutely unfair to the 100-percent reserve. Do you object to that?

Mr. **Ford**. I would not object.

Mr. **Cromwell**. In view of our short time, might I suggest again that that be inserted into the record, and that we give each member a copy of it?

(The answer submitted by Mr. Czerwonky is as follows:)

The plan of preventing the haphazard expansion and contraction of our flow of dollars by compelling all banks to maintain 100 percent in cash behind their demand deposits, has been widely discussed and advocated by some of our more forward-thinking economists. The genesis of the plan is recognition of the fact that the unjustified expansion and contraction of our dollar flow is the chief cause of depressions. The 100 percent cash reserve advocates contend that their plan would be of inestimable benefit to the Nation for three important reasons:

First, that contractions of our dollar flow would be rendered impossible and that disasters such as this present depression could, therefore, never recur.

Second. That wholesale failures caused by runs on banks would be prevented and that demand depositors could never again lose their money.

Third. That banks could no longer originate new money by creating new demand deposits and that the national flow of money would be regulated by confining issuance to a central monetary authority.

Under the 100 percent reserve plan our commercial banks would perform about the same functions as do our present savings banks, excepting that the former might continue to clear checks. In other words, they would receive the savings of some citizens and lend them to other individuals or corporations, at a profit both to their depositors and to their stockholders. But since no part of the funds of demand depositors could be loaned out, and since banks could therefore not earn a profit on such deposits, a charge would, of course, have to be levied against check-money accounts to cover the costs of clearing.

Having briefly set forth the three chief advantages of the 100-percent plan and described how our banks would function under it, let us now discuss some of its disadvantages. Most experts agree that the period of transition from a fractional to a 100-percent reserve system might dangerously disorganize both our banking and our economic systems. This is because our present fractional system provides that member banks must maintain a 10-percent cash reserve, so that the remaining 90 percent of the earning assets, now held as collateral to safeguard demand deposits, would have to be replaced with currency. For the sake of simplicity we have assumed that a straight 10-percent reserve was required for all member banks. As a matter of fact, however, there are three distinct requirements for reserve ratios, under the Federal Reserve Act, depending upon the location of the banks involved. These are as follows: Banks in the central reserve cities 13 percent; in reserve cities, 10 percent, and in other localities 7 percent. Under authority conferred upon the Board by the Banking Act of 1935 these reserves can be doubled at the discretion of the board. Three proposals have been suggested by means of which currency could be substituted for these earning assets and the transition from a 10-percent to a 100-percent cash reserve system thereby effected. Let us describe these three proposals and point out the difficulties which each would entail.

1. It has been proposed that the Government should supply the needed 90-percent cash reserves by taking a lien on the earning assets now held as collateral against demand deposits. Under this proposal the following difficulties would arise:

(*a*) In the event of mismanagement and possible failure of any bank, demand depositors would receive their money in full and the Government would suffer whatever losses occurred. Since, therefore, this proposal would be equivalent to the Government guaranteeing all demand deposits, it would naturally require intensive governmental supervision and regulation of bank loans and policies and would thus engender the very factor of bureaucratic interference which we are seeking to avoid.

2. It has been proposed that the Government should supply the needed 90-percent cash reserves by purchasing from the banks their holdings of Government securities. Under this proposal the following difficulties would arise:

(*b*) Since the prime assets of the banks would be taken over by the Government, the funds of time and savings depositors might be jeopardized because probably only inferior collateral would be left to protect such deposits.

(*c*) Many banks might liquidate due to inability to earn a fair profit. This would not only represent an incalculable loss to the communities so affected but might jeopardize our entire banking system and the $6,000,000,000 invested in it.

(*d*) The use of check money, the most efficient medium ever devised for transacting business, would be discouraged by the levying of charges to cover the costs of clearance. This retrogressive step has already developed to a considerable extent, for, according to Governor Eccles, "The use of the check has been greatly diminished as a result of service charges and the check tax."

3. It has been proposed that the Government should supply the needed 90-percent cash reserves by what corresponds to a combination of proposals 1 and 2, i. e., that to prevent injury to time and savings depositors the Government should take over both prime and poor assets. Under this proposal, however, all the difficulties described in A, B, C, and D would more or less obtain.

Although the 100-percent reserve plan is constructive in theory and worthy of consideration, we contend that the advantages of the plan herein proposed would exceed those offered by the 100-percent reserve plan, while wholly avoiding the disadvantages, i. e., it would bring about dollar expansions easily and quickly to any extent desired and would prevent contractions in the flow of money without, at the same time, interfering in the slightest degree with the functioning of our existing banking system. Furthermore, it is evident that the 100-percent reserve plan offers no direct solution to the grave problems of our vast unemployment and wasted productive capacity. The power to stimulate employment by encouraging our banks to grant loans to productive enterprise, either by reducing reserves or through inducement loans, could not be applied, and grants to the Treasury, which as we explained in section 48, would ordinarily be employed under the proposed bill to supplement the two powers just mentioned, would be the only method, under the 100-percent reserve plan, of attaining and maintaining business stability and full employment. Because the 100-percent reserve plan would, of course, automatically prevent the expansion of demand deposits through loans and investments by commercial banks.

When we consider, moreover, that under the proposed bill, a sharp reduction in taxes on finished consumer goods could be effected by substantial grants to the Treasury simultaneously with the extension of 10-year loans carrying a subsidized profit, there can be no doubt that our economy could always be stimulated into immediate recovery. By the same technique the Board could, of course, positively prevent any lapse in business activity which might result through fears arising from adverse conditions abroad or for any other reasons.

Mr. **McGranery**. I would like to ask the witness a question in connection with this subsidy. Would he say that the United States Steel Corporation, which recently made a loan for $175,000,000, or more, would be entitled to receive the benefits of this subsidy?

Mr. **Cromwell**. Yes; they would.

Mr. **McGranery**. And you believe that that would be good business?

Mr. **Cromwell**. Yes; that would be good business, to encourage any producer who will employ labor.

Mr. **McGranery**. Notwithstanding that the United States Steel Corporation can stand on its own feet without negotiating that loan?

Mr. **Cromwell**. I would still believe that the United States Steel Corporation or any corporation that can prove to the bank or to the Federal Reserve Board that their loan will be used to increase production and employment should be granted inducement loans if they want them.

Mr. **Czerwonky**. May I add a word there on that same question, on the inducement loans?

There is not within our commercial bank structure today a shortage of available funds; in other words, the member banks have about $1,300,000,000 in excess reserves, so the extension of a loan to the United States Steel Corporation, such as you have mentioned, would in no case create a hardship for other private borrowers.

Mr. **McGranery**. But you are taking from the general taxpayer the subsidy which will be of benefit to the United States Steel Corporation.

Mr. **Czerwonky**. I do not know whether you were here while the statement was being read, but the actual subsidy would not be paid by the taxpayers at all. In other words, if you have that statement in front of you there on the money supply in the United States, it shows that the net additions in demand deposits over a period of about 8 years averaged around $750,000,000. Now, the subsidies would be paid out of those net additions which otherwise would be credited to the Treasury. There would be no taxation on the community for these subsidies.

Mr. **Crawford**. Referring to this table you called to our attention a while ago, where demand deposits dropped $7,600,000,000, would you say that that was due pretty largely to the fact that bank management wanted to put itself in position to meet the demands and withdrawals of customers?

Mr. **Cromwell**. Yes.

Mr. **Crawford**. Then would you also take the position that one of the big questions before us today is whether or not the whole monetary and credit mechanism is to be operated in order to enable people to go to the bank and withdraw their deposits, or is it to be operated for the specific purpose of promoting production and employment and the flow of goods to the people of the country? Have we got to face that issue?

Mr. **Cromwell**. I think that Mr. Luce has brought that issue out, but I may say that we can do both, that we can make it perfectly satisfactory.

Mr. **Crawford**. Would you say that heretofore the conservative bankers, whom I respect as much as anyone, because I have extended a few credits in my life, and my losses did not extend over one-tenth of 1 percent per annum, but would you say that heretofore the conservative banker has had to keep in mind all the time that his obligation was to be able to meet the withdrawals of depositors, and that has been his primary objective, and that is the primary objective of the commercial banker today, but in doing that would you say that it leaves the rest of the world in a position where it cannot function?

Mr. **Cromwell**. That is absolutely correct.

Mr. **McKeough**. In your approach to this solution, I presume that you have given some thought to the production of the country on a long-term average of years, and to that part of it which would be exported? In other words, in your approach to this problem, have you considered the possibility of eliminating that measure of the production that represents exports of our products?

Mr. **Cromwell**. No; I have not considered any elimination of exports. In fact, I assume that if we were able to increase our domestic production, our export business would increase proportionately.

Mr. **McKeough**. You consider, then, that this increase of production would not necessarily have to be entirely consumed here?

Mr. **Cromwell**. No; I think it would be chiefly consumed here, but I think that our import and export business is entirely dependent upon the amount of business done within our country. As the business within our country expands, so will our import and export business expand. The one is attached to the other.

Mr. **McKeough**. Getting back to Mr. McGranery's question of the United States Steel Corporation borrowing directly from the commercial bank, that in itself would be an argument in defense of your theory, by reason of their ability to get a commercial bank loan instead of floating long-term loans through investment banking facilities; but what I am wondering about is whether or not the question of production is not secondary to the ability to consume in this country. We are told that there are one-third of our people that are ill-clad, ill-housed, and ill-fed. If that is the situation, I do not believe that it is a requirement so much of added production until at least such time as the underconsumptive power is raised to meet the productive power that now exists, and I am just wondering whether or not this scheme of yours is giving consideration to the feature of raising the consumptive power now—not tomorrow or the next day. How do you approach that in your study?

What is your answer to that difficulty? It apparently is the most terrible problem that we have to meet. If we can raise our consumption, we can raise our employment. Certainly there is not any absence of an ability to produce. The steel industry is now borrowing money—90 percent for the purpose of improving existing plant facilities and 10 percent for expansion of existing facilities—and with these technological improvements, fewer people are required in order to produce a larger production. There is no absence of ability on the part of the steel industry of the United States to meet what up to now has been the total largest single consumptive requirement; in fact, there is probably an ability to reduce the existing production of steel to 40 percent and still have with the remaining plant facilities sufficient productivity to meet the present largest consumptive requirement in any given period.

So I am wondering how we will cure that situation that now prevails.

Mr. **Transue.** What you are saying is, what business wants are customers.

Mr. **McKeough.** Exactly.

Mr. **Transue.** And the customers have to have the money to buy the goods.

The **Chairman.** Of course, these gentlemen think that they have the answer to that.

Mr. **McKeough.** I am sorry that I was not here for all of this discussion.

The **Chairman.** Whether they have it or not, I do not know.

Mr. **McKeough.** If they have, I am for them.

Do you think that you can give me a brief answer to that long question?

Mr. **Cromwell.** I would say that there are two methods to increase the purchasing power included in our recommendations. The first method of increasing mass purchasing power would be the power granted to the Board of Governors to make grants to the Treasury, which is the same thing as reducing taxes. When you reduce taxes—that is, excise taxes—you at once proportionately increase the purchasing power of the masses.

Is that right?

Mr. **McKeough.** Well, I think that that is purely academic, but go ahead.

Mr. **Cromwell.** No; that is not academic.

The **Chairman.** I am sorry, gentlemen, but there is a roll call on in the House, and the Members must answer it.

We thank you, Mr. Cromwell. We shall be glad to have you with us again at any time you can get here.

[Mr. Cromwell left for the record, as part of his statement, the material appended hereto as exhibit A.]

(Thereupon, at 12:20 p. m., an adjournment was taken until Friday morning, February 11, 1938, at 10:30 o'clock.)

EXHIBIT A

OBJECTION TO GRANTS TO THE TREASURY ANSWERED

The chief objection to authorizing the Board to make grants to the Treasury is probably that this power might be abused for political purposes, i. e., because the Board is appointed by the President with the consent and approval of the Senate, and because the coinage and regulation of the Nation's money would be placed in governmental rather than private hands. With gold restrictions upon monetary expansion abolished, furthermore, orthodox economists and the old school of businessmen, as well, may condemn this proposal as one which would lead to inflation and economic chaos.

In the first place, the tenure of office of Governors of the Board, under the Federal Reserve Act, is expressly designed to prevent any single administration from obtaining control of the Board through the appointive power. It seems safe to assume, therefore, that the Board would normally be independent of political pressure in reaching its decisions and would be accountable to Congress and to the public only in submitting full and open reports of how and why its policies were determined.

In the second place, additions to the flow of dollars which could be made by the Board through grants would be limited to such sums as might be required to offset the increased flow of finished consumer goods. Since, as we have just stated, the reasons which prompt the Board to reach its decisions must be made public, it would seem most unlikely that the Board would ignore its statistical indicators and deliberately adopt a policy of inflation to please an administration which would hold no punitive power, such as removal, over its members. It must likewise be borne in mind that the Board has no responsibility so far as the fiscal administration of the Government is concerned. Its sole responsibility should be to maintain synchronization and business stability and it could not be compelled to disregard the specific mandates imposed upon it by the proposed bill except by act of Congress.

In the third place, since the duty of the Board should be to maintain business stability and thus protect those engaged in sound commercial enterprise, we contend that providing the Board with power to employ either one or both of two positive methods of augmenting the flow of dollars (i. e., to make grants and to authorize inducement loans) represents the logical and proper fulfillment of one of the most vital obligations of our Government to the people. Without this power our commercial banks would hold the upper hand in the matter of making dollar additions and the public welfare could be jeopardized by any one of or a combination of such possible occurrences as we shall now set forth. We trust that critics of our recommendations will carefully consider these possible threats to the public welfare. If better methods can be devised to safeguard national interests than those we propose, such methods should, of course, be adopted. If not, we believe that the following discussion will convince unprejudiced readers of the necessity for authorizing the Board to make grants to the Treasury.

1. Suppose that under normal conditions the Board used the second method of augmenting the dollar flow and reduced the reserve requirements of our commercial banks in the anticipation that they would expand their loans to industry. And suppose that despite the protection afforded by this bill against heavy demands for currency during periods of emergency, our banks nevertheless resolutely refused to extend loans to businessmen for sufficient lengths of time to assure the latter of full independence and to permit gradual repayment out of earnings. Now, simply because their refusal might be based upon the tradition that bank loans should be extended for periods preferably under 90 days and were over a year or two, because of such an obsolete tradition should the Board be left powerless to augment the dollar flow and to safeguard the public welfare.

We contend that if the banks refused to extend loans of such duration to businessmen as would conform to the requirements of the latter (within the provisions of this bill) the Board should be empowered to make grants to the Treasury and thereby to augment the dollar flow as required. Since augmentation through grants would increase the deposit liabilities of the banks without increasing their earnings, it is highly probable that the banks, being aware of such a contingency, would discard their obsolete traditions and meet the requirements of business in order to gain new customers and earn a profit on additional loans. Through the power to make grants, therefore, the Board, in this instance, would have been able to have influenced the modernization of the lending policies of our commercial banks and would thus have benefited the businessman, the banker, and the general public.

2. Suppose that the Board should again use the second method in the endeavor to augment the dollar flow, and that in this instance the banks, instead of extending new loans which would directly increase the demand for finished consumer goods, should grant loans for speculative purposes, or should purchase outstanding corporate and governmental bonds. Providing a bondholder with dollars in exchange for his collateral does not positively assure added demand for finished consumer goods. The newly acquired dollars may remain idle, or, as already stated, be used to bid up the price of "listed" securities. Under such circumstances should the Board be left powerless to synchronize the increased flow of goods with consumer dollars and to protect the public against speculation and idle money?

We contend that the Board should inform the banks that the use of the additional reserves for speculative purposes or to buy outstanding obligations would be contrary to sound monetary policy; that to counteract such a tendency, the Board should be able to raise reserves to the former level, and that the Board should be able to synchronize dollar flow with goods flow by making grants to the Treasury. When the Board refrained from augmenting the dollar flow through grants, and instead permitted the banks to make dollar additions by lowering reserve requirements, such action would represent a gift to the banks and it would certainly not be unreasonable for the Board to insist that such gifts should not be abused. Had the Board been equipped with these powers in 1929, excess reserves could have been created without fear that additions to the dollar flow would have been diverted into speculative channels. The inherent weakness in open-market operations has always been that the funds created might be used for speculative purposes.

It must be clearly understood that the responsibility of the Board does not end when commercial banks expand their loans. The Board must be certain that the new dollars are placed in the hands of those who will use them to buy the increased flow of finished consumer goods which necessitated the augmentation. The new dollars, therefore, must either be directly employed by the recipients to buy consumer goods or transferred by investment (i. e., through the payment of wages and salaries) to others who will so employ them. Obviously, if the new dollars were used to bid up and exchange outstanding obligations, or if they remained idle, synchronization would not have been maintained.

3. Suppose that the subsidy required to persuade businessmen to increase their borrowing through inducement loans was greater than seemed sensible and reasonable. Should the Board, in this case, be left powerless to protect the public interest?

4. Suppose that under abnormal conditions, such as exist today, the commercial banks were unwilling to extend inducement loans unless they were paid service charges which seemed unreasonable from the standpoint of the public interest, i. e., suppose for example that the banks demanded a 5, 6, or 7 percent service charge to extend subsidized loans which appeared safe and beneficial while, at the same time, they were satisfied with a 3-percent return on Government bonds. Should not the Board be empowered to safeguard the public welfare by making grants to the Treasury as in the first supposition?

And should the Government, in order to maintain business stability and full employment but to escape excessive service charges, be compelled to unbalance the Budget, and to incur interest-bearing deficits? Should the Government, in other words, be compelled to increase the national debt, when one of the chief objectives of authorizing the Board to make grants would be to avoid the necessity for such borrowing? If it is necessary to augment the national flow of money, why should the Government be forced to sell its securities to the banks to get money and to put the new funds into circulation through public works expenditures, when augmentation could be achieved far more rapidly, cheaply, and efficiently through grants by the Board to the Treasury? (See part IV, diagram 5, for further discussion of this subject, In Defense of Capitalism.)

Today our banking system holds about 46 percent of the Federal debt and our commercial banks, instead of fulfilling their proper role as "merchants of credit" to industry and agriculture, have largely become buyers of bonds, primarily Federal obligations. Because of the failure of our banks to offer attractive loans to private enterprise and because businessmen are unwilling to subject their concerns to the uncertainties of short-term loans and banker domination, they have naturally come to prefer and seek permanent public financing. The cessation of further Federal debt issuances, combined with the liquidity of productive loans provided by these amendments should, however, induce bankers to offer business concerns loans of intermediate duration and thereby permit our commercial banks to resume their proper role within the economy.

By intermediate financing is meant loans up to 10 years' duration as distinguished from long-term loans or bond issues for over 10 years' duration and from short-term loans under 2 years' duration. With an unregulated money system it would have been dangerous for banks to grant intermediate loans due to the uncertainty of business conditions. With a scientific money system, however, such uncertainties would no longer exist, and commercial bankers could safely and effectively compete with investment bankers to furnish the funds required by businessmen.

We have endeavored to point out the fact that synchronization required that the Board be equipped with positive means to augment the dollar flow, and that if synchronization cannot be maintained, our economy will be subjected to permanent unemployment, increasing Government interference and depression of such intensity as might engender the ultimate destruction of capitalism. The question is, therefore, Are the American people willing, because of archaic misconceptions and traditions, to sit idly by and witness a series of worse catastrophes than the 1929 depression or do they prefer to adopt scientific methods which should prevent such catastrophes from occurring?

There is no middle road! Either we must insist that Congress cease flouting the Constitution and carry out, through its agency the Board, the specific mandate to "coin and regulate the value of money" or we must supinely resign ourselves to the fatal eccentricities of an unregulated money system. Since the present system has so painfully proved that it leads to economic chaos, we contend, of course, that it would be wise to modernize it and to set another course, which at least, would not be certain to cast our economic ship, for the fifteenth time since the Declaration of Independence, upon the same rocks. In conclusion it is, of course, obvious that the reader himself must determine the answer to this question, Is it the part of wisdom to refuse an administration the liberty to render a positive service because that liberty may be abused?

BRIEF OUTLINE OF THE PROCEDURE INVOLVED IN OBTAINING "INDUCEMENT LOANS"

The Board would establish, from time to time, the interest rate and the service charge on loans which qualified as "inducement loans." By this authority the Board, through the commercial banks, could vary the terms of lending so that borrowers would be responsive and increase their total dollar borrowings until the dollar flow had been sufficiently augmented.

A bank would present for certification to the loaning officer of the Reserve bank of its district, four copies of the loan it proposed to make to its customer and would attest that the loan was to be used for increasing the rate of productive activity. These copies would have to be notarized before being presented to the Reserve bank, on forms furnished by the Reserve bank. Upon receipt of the forms by the Reserve bank they would be stamped with the date, the interest rate, and the service charge to which the loan was entitled; provided, of course, that the loan was accepted, i. e., certified, by the Board or its duly appointed agent at the Reserve bank. After certification by the Reserve bank two copies of the loan would be retained by the Reserve bank (one being held by the Reserve bank and the other being forwarded to the Board) and two copies would be returned to the member bank, one for its own records, and the other for the records of the bank's customer.

At semiannual or annual intervals the member bank would receive by check from the Board, or its duly appointed agent, the subsidy and the service charge (possibly only the latter would be involved) which such bank was entitled to receive.

The business qualifications and character of the bank customer would not be of concern to the Reserve bank personnel engaged in the certification of loans, and the Board would assume no responsibility beyond the interest and service charge which it authorized. Upon evidence, however, that the bank's customer was using the funds acquired under the title of "inducement loans" for purposes other than what was agreed upon, the Board would be authorized to discontinue the subsidy and service charge, and to make such assessments against the member bank involved as would reimburse the Board for the interest and service charge which had been falsely obtained.

ARE NONMEMBER BANKS COMPELLED TO BECOME MEMBERS?

The proposed amendments do not require that State banks, which handle checking accounts, shall be compelled to become members of the Federal Reserve System or comply with provisions covering minimum capitalization, etc. According to section 4-B, however, State banks would be required to keep their legal reserves against checking accounts on deposit with the Federal Reserve bank of their district, and they would be subject to such rules regarding reserves as might be prescribed by the Board. Since reserves control the volume of check money, it is obvious that the above requirement is essential if the Board is to fulfill the duty of regulating our national flow of dollars.

This requirement, however, would not impose any hardship upon nonmember banks, because they do not receive, at the present time, any interest on their legal reserves held in the form of demand deposits with member banks. The Banking Act of 1933 forbade the payment of interest on all demand deposits, including interbank deposits—and this rule was incorporated into the Federal Reserve Act. Section 19, paragraph 12. Furthermore, the transference of these reserve deposits from member banks to Federal Reserve banks would not necessitate the calling of loans by such member banks (which would cause a contraction of dollar flow), because practically all member banks now have appreciable excess reserves.

We hope that the plan of inducement loans, and other advantageous measures provided for in the proposed bill, would, if adopted, convince nonmember State banks of the desirability of becoming member banks, and that our financial system might thereby achieve complete unification. To encourage and facilitate unification it is recommended that the paid-in, capital required for eligibility be reduced to the minimum consistent with safety. It might be possible, furthermore, to admit to membership banks deficient in capital, provided they would undertake to make up the deficiency within a period of 10 years.

Supervision of nonmember State banks would continue under the jurisdiction of State banking commissioners and State examiners, although State banks applying for membership would be subject to examination before admission by the district Federal Reserve bank, in accordance with regulations.

OMISSION OF PRICE-LEVEL INDICATOR EXPLAINED

Disciples of the price-level school of managed money will doubtless note that no mandate is called for which would direct the Board to restore and maintain, for example, the 1926 price level as designated by our Bureau of Labor Statistics. The ability of a nation to manage its money so as to maintain the stability of a weighted index number or price level may be granted, provided that the central bank authorities are equipped with positive monetary controls. The Swedish Riksbank, the pioneer of money management by price level, set up a price-index system in 1930 and has succeeded in maintaining price-level stability except for insignificant fluctuations. It may likewise be granted that such a monetary gage is far better than arbitrarily regulating the flow of money by the gold reserves held in the central bank. Certain leading mathematicians in recent writings, however, hold that price-index numbers are mathematically invalid, have no economic significance, and are dangerously misleading as a guide to monetary policy. But is price-level stability an accurate and sensitive gage of business stability in our modern investment economy?

In the first place, if goods began to be hard to sell because of an insufficient flow of money, would merchants cut prices and take a loss or would they reduce the quantity or reorders from factories? It is most likely that merchants would resist losses, would endeavor to maintain prices, and would reduce reorders. To that degree, therefore, price indexes may be defective in promptly indicating recessions in production and employment.

In the second place, would manufacturers reduce prices on goods offered to merchants, even suffering a loss in order to maintain their rate of activity, or would they curtail production and attempt to maintain prices? We believe the latter course has been generally substantiated by experience.

The services of an executive whose company was doing a large volume of business without profit would not be satisfactory to his investors. The executive, therefore, would naturally prefer to discharge workers and do a lesser volume of business at a profit. If a profit could not be earned he might operate at a greatly reduced rate and suffer a small loss as long as his cash reserves permitted, in order to meet the cost of taxes, insurance, interest, and other fixed charges. The effect, of course, would be involuntary unemployment in the face of price index stability.

The chief intent of this bill is to restore and maintain full employment, for unless citizens able and willing to work can obtain employment, the capitalistic system is a failure and our so-called economy, of abundance is false. With this intent in mind it would seem that such a gage as man-hours of employment would be more sensitive and accurate than price level indexes.

To repeat again, all wealth is produced from the earth by capital and labor, i. e., savings and productive facilities combined with man-hours of employment. The fundamental yardstick of goods flow, therefore, should be man-hours of employment because a decrease in man-hours would indicate a decrease in goods flow. Objections might be raised to this yardstick on the grounds that technological unemployment would render it inaccurate, but the total volume of production in America is so vast that the effect upon employment of such technical improvements as might be instituted within a year's time, would be infinitesimal. Technological unemployment, furthermore, is never permanent, and under a scientific money economy operating at full capacity, displaced workers would find plenty of jobs available in other fields of activity.

It is anticipated that businessmen who were cognizant of the vital importance of providing accurate indicators to guide the Board, would willingly cooperate to the extent of supplying the Board with confidential monthly or quarterly reports setting forth their man-hours of employment and the dollar and physical volume of their production. Cooperation by the leading industries of the Nation, combined with reports from the county agents of the Department of Agriculture, would probably provide sufficiently comprehensive and reliable data to permit the Board promptly to detect the inception of any recession in business activity. It is desired in this bill to avoid any semblance of coercion, but should voluntary reports prove insufficient, Congress could doubtless enact legislation which would compel all labor-employing enterprises in the Nation to submit accurate confidential reports to the Board. As was stated in the preceding paragraph, however, other mathematically valid indicators would be used in conjunction with man-hours of employment to detect any signs of maladjustment between production and consumption.

WEAKNESS OF OPEN-MARKET OPERATIONS EXPLAINED

By open-market operations is meant the purchase by the Federal Reserve banks, in the open market, of certain types of securities, primarily Government bonds, from commercial banks, corporations, or individuals. The purpose of the purchase of these obligations is chiefly to provide commercial banks with excess reserves at the Reserve banks. The existence of these excess reserves permits commercial banks to expand their loans and investments and with it the flow of dollars. As stated previously, "the primary function of reserves is to control the volume of demand deposits or check money."

But whether the desired expansion of dollar flow actually takes place, obviously depends upon the willingness of commercial banks to expand their loans under prevailing conditions and upon the willingness of borrowers to increase their borrowings from commercial banks. In the absence of the ability of the Board to make grants to the Treasury, open-market operations are as ineffective as, and even more subject to speculative abuse than, the second method we have suggested for augmenting the dollar flow, i. e., lowering reserve requirements. In both cases, therefore, the Board would be virtually helpless without the power to make grants and the commercial banks would hold the upper hand in determining whether or not dollar additions would take place. Since the Board cannot influence the banks to extend the type of loans required by businessmen through open-market operations, it can merely make excess reserves available and hope that an expansion of the dollar flow will take place. As Governor Eccles testified before the Committee on Banking and Currency of the House of Representatives, "There is no action that the Board itself can take that will induce individuals and corporations to borrow the excess funds which the banks may have as a result of the Board's action in creating these excess funds."

Conversely, open-market operations can be used to reduce member bank reserves by selling securities in the event that such reserves become excessive through gold inflow.

EXPLANATION OF THE MECHANICS OF GRANTS TO THE TREASURY

Provided that dollar additions were warranted by an increased flow of finished consumer goods within the Nation, which is the only economic justification for the local origination of dollars by commercial banks, the Board would write out checks against deposit credits which the Board itself created. The checks would be made out to the Treasury and forwarded to this body.

Since the Federal Reserve banks are the fiscal agents of the Government these checks, when endorsed by the Secretary of the Treasury, would be deposited at the various Reserve banks and credited to the account of the Treasury. The Treasury would then make disbursements out of these accounts and the Treasury checks would be deposited by the recipients in their own neighborhood banks. Demand deposits would thus be increased and the endorsed checks returned to the Reserve banks and credited to the reserves or balances of the member banks. When the original checks sent to the Secretary of the Treasury were returned to the Board by the respective Reserve banks, they would receive a deposit credit on the books of the Board and the accounts of the Reserve banks would thereby be balanced. These deposit liabilities of the Board to the Reserve banks would be permanent because there would never be any justification for contracting the flow of dollars unless the flow of finished consumer goods was likewise contracted. All such creations of new money would be put into general circulation by bookkeeping entries in ledgers and by means of those slips of paper we call checks. It should be emphasized that no paper currency would be printed.

OBJECTIONS TO BALANCE SHEET WITH UNBALANCED LIABILITIES ANSWERED

An objection which may arise with respect to the monetary mechanism proposed herein is that a balance sheet with unbalanced liabilities has never been heard of. We refer, of course, to entries on the books of the Board, which would record the extension of grants to the Treasury and inducement loan credits.

When grants were made to the Treasury, or subsidies were paid to private individuals and banks as a result of inducement loans, the books of member banks and the Federal Reserve banks would automatically balance. The increased liabilities of member banks would be balanced by the increased liabilities of the Reserve banks to such member banks, i. e., member banks would hold credits on the books of the Reserve banks. Similarly the increased libilities of the Reserve banks to member banks would be balanced by the increased liabilities of the Board of Governors to the Reserve banks, i. e., the Reserve banks would hold credits on the books of the Board. At this point the question would arise as to what would balance the liabilities of the Board of Governors. The answer is that this body would be acting as a bank of issue for the Nation and the assets which would balance its liabilities to the Reserve banks would be the increased flow of finished consumer goods within the Nation.

So long, therefore, as the flow of finished consumer goods was maintained, the liabilities of the Board would be properly balanced, and they could not be called unbalanced liabilities except in the most narrow bookkeeping sense, i. e., in the sense that the Board would hold no paper, liquid or nonliquid in nature, as assets to offset the deposit liabilities to the Reserve banks.

It may assist the reader to concur in the economic validity of this procedure by imagining that the Board was the administrator of a huge corporate body, the Nation, to whose central marketing organizations were being delivered all finished consumer goods, in return for which the Board was giving to the various producers a book credit subject to transfer by check. When the weekly flow or receipt of finished consumer goods to the marketing organizations increased, as the result of the indirect investment process, the demand deposits or credits which were originated by the administrators, i. e., the Board, would automatically be expanded. Surely no one would question the validity of the increased demand deposits or liabilities which were originated, if the imaginary conditions set forth above actually existed, inasmuch as the added current demand deposits or credits would be balanced by the increased current receipt of finished consumer goods. Similarly, the demand deposit expansion effected by the Board, through grants or subsidies, which would result in increased deposit liabilities of the Board to the Reserve banks is intended to balance an increased flow of finished consumer goods to the markets of the Nation.

PERTINENT QUOTATIONS FROM ECONOMIC TEXTBOOKS

The classical economists, and for the most part the orthodox economists of today, maintain that production of goods in general in excess of the means of payment is impossible. A deficiency of purchasing power, in other words, is absurd; cannot occur. These economists do not recognize the necessity today of adhering to a definite monetary pattern in order that the profitableness of business as a whole may be maintained. They contend the volume of purchasing power and the volume of goods in general offered for sale automatically balance. The following quotations not only substantiate this, but in addition display the theory of the working of capitalist enterprise as they visualize it.

John Stuart Mill: Principles of Political Economy, 1921 edition, pages 557–558:

"* * * let us suppose that the quantity of commodities produced is not greater than the community would be glad to consume; is it, in that case, possible that there should be a deficiency of demand for all commodities for want of the means of payment? Those who think so cannot have considered what it is which constitutes the means of payment for commodities. It is simply commodities. Each person's means of paying for the productions of other people consists of those which he himself possesses. All sellers are inevitably and ex vi termini buyers. Could we suddenly double the productive powers of the country, we should double the supply of commodities in every market; but we should, by the same stroke, double the purchasing power. Everybody would bring a double demand as well as supply; everybody would be able to buy twice as much, because everyone would have twice as much to offer in exchange.

"A general oversupply, or excess of all commodities above the demand, so far as demand consists in means of payment, is thus shown to be an impossibility."

Ricardo: Principles of Political Economy, chapter XXI:

"Productions are always bought by productions, or by services; money is only the medium by which the exchange is effected. Too much of a particular commodity may be produced, of which there may be such a glut in the market, as not to repay the capital expended on it; but this cannot be the case with respect to all commodities. * * *"

Dr. Alfred Marshall: Principles of Economics, sixth edition, Book VI, chapter XIII, pages 710–711, footnote:

"The quotation from Mill and the two paragraphs which follow it * * * indicate the attitude which most of those who follow in the traditions of the classical economists, hold as to the relations between consumption and production. It is true that in times of depression the disorganization of consumption is a contributory cause to the continuance of the disorganization of credit and of production. But a remedy is not to be got by a study of consumption, as has been alleged by some hasty writers."

Prof. F. W. Taussig: Principles of Economics, second edition, volume II, page 50:

"The process of investment by the well to do simply means that the 'consuming power' is turned over to the laborers. There is no lack of consuming power. If, indeed, this process goes to its limit, if the investors persist in saving willy-nilly, the ultimate result must be overproduction in the sense of disappearance of profit or interest. But this limit will never be reached. Long before it is approached, an end will come of the excessive investment; demand will be readjusted, and the various sorts of goods will be turned out in such apportionment that (barring the inevitable occasional mistakes) all will be sold at a profit."

Prof. F. W. Taussig: Op. cit. page 47:

"In all this reasoning (on overproduction) there is confusion of two essentially different things; on the one hand, investment beyond the point where a return to capital can be maintained; on the other hand, production beyond the point where a market for goods can be found. The first of these is quite conceivable, though highly improbable. The second, so long as human wants remain extensible, is not conceivable."

Joseph Schumpeter: The Explanation of the Business Cycle, Economica, December 1927:

"The problem of the business cycle * * * presented itself to the economists of the classic period and their immediate successors in the aspect of the striking fact of recurring 'crises.' Two first results were speedily established. The one, negative only but of the greatest 'diagnostic' importance, was that there can be no such thing as a general glut. * * *"

Prof. Gustav Cassel: The Problem of Stabilization, Scandinaviska Kreditaktiebolaget, January 1929, page 3:

"When in popular discussions people argue about the insufficiency of purchasing power, they are, however, sure to be on the wrong track, and are apt to be led into the most absurd conclusions. The purchasing power of the community can never be anything but the value of the total production of the community, and, therefore, cannot develop at a slower pace than the latter."

J. A. Hobson: Economics of Unemployment, page 69:

"Is there any reason why * * * full employment at high prices with high profits and high wages should not continue indefinitely? Only one, viz, a failure to sell at the current high prices the whole supply of final commodities which the whole process of production is capable of putting into the markets. Now it is admitted that all these final commodities could be sold, in the sense that someone possesses the money income capable of buying them."

J. A. Hobson: Rationalization and Unemployment, 1930, page 6:

"The failure of the expansion of markets is manifestly the crux of the situation. It cannot easily be attributed to a lack of purchasing power. For the income paid in rent, wages, interest, profits, salaries, in the various processes of producing wealth ought, prima facie, when added up, to make the sum needed to purchase all the goods, if it is used without undue delay in buying goods, the only use to which it can be put."

John A. Hobson: The Manchester Guardian Weekly, January 16, 1931, page 57:

"There is a chronic attempt to oversave income, checked by the disastrous discovery that the goods which represent the oversavings lie for a long time unutilized. * * * The futile and costly attempt to oversave is due to an irrational and inequitable distribution of income. * * * This "irrational" element, introduced into our economic system by maldistribution of income, shows itself later on in the irrationality of general unemployment, the inability of consumption to keep pace with productive power."

John Maynard Keynes: The General Theory of Employment, Interest, and Money, pages 240 and 242:

"That the world, after several millennia of steady individual saving, is so poor as it is in accumulated capital assets is to be explained, in my opinion, neither by the improvident propensities of mankind nor even by the destruction of war but by the high liquidity premiums formerly attaching to the ownership of land and now attaching to money.

"The order of preference in the minds of owners of wealth in which at any time they express their feelings about liquidity is, however, definite and is all we require for our analysis of the behavior of the economic system."

Adams Smith: The Wealth of Nations:

"It is the great multiplication of the productions of all the different arts, in consequence of the division of labor, which occasions, in a well-governed society, that universal opulence which extends itself to the lowest ranks of the people. Every workman has a great quantity of his own work to dispose of beyond what he himself has occasion for; and every other workman being exactly in the same situation, he is enabled to exchange a great quantity of his own goods for a great quantity, or what comes to the same thing, for the price of a great quantity of theirs. He supplies them abundantly with what they have occasion for, and they accommodate him as amply with what he has occasion for, and a general plenty diffuses itself through all the different ranks of the society." Page 13.

"And thus the certainty of being able to exchange all that surplus part of the produce of his own labor, which is over and above his own consumption, for such parts of the produce of other men's labor as he may have occasion for encourages every man to apply himself to a particular occupation and to cultivate and bring to perfection whatever talent or genius he may possess for that particular species of business." Page 17.

"When the division of labor has been once thoroughly established, it is but a very small part of a man's wants which the produce of his own labor can supply. He supplies the far greater part of them by exchanging that surplus part of the produce of his own labor, which is over and above his own consumption, for such parts of the produce of other men's labor as he has occasion for. Every man thus lives by exchanging, or becomes in some measure a merchant, and the society itself grows to be what is properly a commercial society." Page 24.

"It is by far the best policy to leave things to their natural course."

"There will always be plenty of money if things are left to their free course * * *."

"Little else is requisite to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice; all the rest being brought about by the natural course of things."

John Stuart Mill:

"If values remain the same, what becomes of prices is immaterial, since the remuneration of producers does not depend on how much money, but on how much of consumable articles, they obtain for their goods."

Dr. Alfred Marshall: Principles of Economics, page 581:

"Everyone is aware that the accumulation of wealth is held in check, and the rate of interest so far sustained, by the preference which the great mass of humanity have for present over deferred gratifictaions, or, in other words, by their unwillingness to 'wait'."

DIFFERENCE BETWEEN ORTHODOX AND REALISTIC APPROACH

(*a*) The former, in the theorizing, disregards the modern business structure, i. e., the impersonal business institutions of today. This involves overlooking the change from the direct individual ownership of the instruments of production to the investor ownership of these instruments.

(*b*) The former ignores the necessity of business enterprises recovering in the prices of finished goods sold the money costs which have been incurred in their production plus a profit.

THE PRICE EQUATION

What all producers of goods, industrial and agricultural, desire in the sale of their goods is a price which will return to them the money costs which they have expended in the production of the goods plus a reasonable profit. Now price is nothing more than the number of money units asked or gained per 1.0 quantity units of some kind of goods. If we let the letter "P" signify a price it is expressed numerically by the fraction M/Q, where M is the number of money units paid for the number of quantity units of some one kind of goods symbolized by Q. Thus for example—

$$P = \frac{M \text{ dollars}}{Q \text{ bushels of wheat}}$$

But as we have repeatedly emphasized, our economic system can only be understood as a thing in motion, not as a thing at rest, i. e., it is necessary to think in terms of flows and not pools, and for this reason it is necessary to recast the previous equation to read as follows:

$$P = \frac{\text{flow of dollars to the market}}{\text{flow of goods to the market}}$$

Now in the presence of perfect market competition, i. e., in the absence of all restraints upon production, this equation would be realistic in adaptation. If, at any moment, we knew the flow of dollars and the flow of goods, the prices of goods would be predictable. But the flow of goods to the market consists of agricultural and industrial products, making the equation read:

$$P = \frac{\text{flow of dollars to the market}}{\text{flow of agricultural goods} + \text{flow of industrial goods}}$$

and in the industrial goods the manufacturers insist on prices which will return them costs plus a profit. If the flow of dollars to the market the numerator of the equation does not enable them to recover money costs, they curtail operations so that on what they do produce they can make a profit. This is what the classical economists completely ignore.

Now we have a choice within our national economy of pursuing three distinct governmental courses. We can, first of all, adopt a policy of laissez faire, i. e., do nothing. Or we can set up a governmental agency which will enable the farmers to regulate agricultural production and gain a decent price, i. e., enable the farmers to do what industry is now capable of doing by itself. Or finally we can regulate the numerator of the price equation, the flow of dollars fo the market, and induce full industrial and agricultural production. Both the numerator and denominator of the price equation are man-made, and it seems to us to be the pathway of wisdom to regulate the numerator.

OBJECTIVE VIEW OF THE PROPOSED AMENDMENTS

To those who concur in the necessity of synchronizing the flow of money with the flow of finished consumer goods, and yet are inclined to view with skepticism the practicability of the proposition of "inducement loans," we recommend serious reflection of the following observation.

There are, in our belief, only three direct ways of bringing about an increase in the flow of money:

First, demand deposits can be expanded and made to flow through increased private borrowing at commercial banking institutions.

Second, demand deposits can be expanded and made to flow through increased governmental borrowing at commercial banking institutions.

Third, demand deposits can be expanded and made to flow through such a method as Mr. Goldsborough suggests of grants to consumers by means of discounts on retail sales, or through such a method as we suggest of grants to the Treasury by the Board. The former involves great administrative difficulties, while the latter, as we have previously explained, involves none.

Now there is, of course, a possibility of influencing and bringing about increased private borrowing at commercial banking institutions by the Government guaranteeing the repayment of the principal as well as the interest of all loans made by private borrowers. This, however, we do not believe to be a sound governmental policy because it injects the Government in a personal relationship in every loan, passing upon the character of the prospective borrower, the adequacy of the security which he offers as cover, the soundness of the business venture, etc. We believe that "inducement loans," which involves none of these factors, guaranteeing only a small subsidy in order to positively bring about increased private borrowing at commercial banking institutions, is a far superior technique.

To comprehend thoroughly the manifold advantages to the Nation which would accrue as a result of promoting recovery by means of "inducement loans" rather than by increased governmental borrowing, we must consider the three most vital factors which are involved in comparing the two methods, i. e.:

1. The efficiency of Federal expenditures.
2. The cost to taxpayers.
3. The loss to the Nation of idle labor and productive facilities.

Assuming that "inducement loans" were extended at a total cost to the Government of 6 percent per annum, as per the example cited previously, every dollar disbursed by the Board would induce an increased actual expenditure by private enterprise of $16. If a service charge of 3 percent to loaning banks should be fixed by the Board, and money were loaned to business enterprises without interest, then every dollar disbursed by the Board would occasion an increased expenditure of $33 by private enterprise. In short, "inducement loans" would promote, at an invisible cost to taxpayers of $1 or less, a far more efficient increase in check-money deposits and employment than work relief would promote by a minimum direct expenditure of $16.

As was explained previously, the cost of "inducement loans" would be in the form of book charges which ultimately would be paid by deductions from grants to the Treasury required by increased production. Taxpayers consequently would bear no burden as a result of these loans, while they would bear an additional burden if increased governmental borrowing at commercial banking institutions took place.

Finally, with "inducement loans," productive capacity and full employment would be achieved both rapidly and permanently. It would incite no psychology of fear in the minds of business men and bankers as increased governmental borrowing and spending does. In contract to a maximum of 15 or 17 thousand governmental spending projects, many of which represent a loss to taxpayers, money could be injected into our economy by the proposed method through loans both to individual producers or enterprisers and to some of our 100,000 or more corporations engaged in producing and distributing goods.

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

FRIDAY, FEBRUARY 11, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 11:05 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Transue, Mr. Gifford, Mr. Luce, and Mr. Crawford.

The **Chairman**. The committee will come to order, please.

We have with us this morning Mr. Herbert Bruce Brougham, an economist, who has been invited to discuss the bill.

I am sure that the committee will be glad to hear you, Mr. Brougham. You may proceed.

STATEMENT OF HERBERT BRUCE BROUGHAM, CONSULTING ECONOMIST, MOUNT VERNON, N. Y.

Mr. **Brougham**. Mr. Chairman and gentlemen of the committee, I appear in an individual capacity on this bill. I have served as secretary of the Pollak Foundation for Economic Research, and I have been associated with Irving Fisher for 6 years and helped him write several of his economic books, including his book on the stock-market crash of 1929.

I have made a special study of the fundamentals of this bill. I believe not only in the objective of this bill but, in the main, I think, the approach to that objective.

I have certain amendments which you might call perfecting amendments to suggest, and I have a statement to submit for the record. I will not read it, if you prefer, and my remarks will be brief, and, by way introduction to the subject matter——

The **Chairman**. Permit me to make a suggestion. It would be better that you let your suggested amendments be the last part of your discussion. In case we do not get to to go into them fully we would not miss as much as if we missed your discussion of the main features and purposes of the bill.

Mr. **Brougham**. I do not want to traverse the territory that Mr. Goldsborough covered.

The **Chairman**. Use your own judgment. That is merely a suggestion of mine. Proceed in whatever way you choose.

Mr. **Brougham**. The amendments introduce a rather large subject, with which I know Mr. Goldsborough is in complete sympathy, for he said to your committee that the ultimate goal of this bill is 100-percent reserves for the banks.

My own main suggestion for an amendment would be to make that mandatory instead of permissive or discretionary, as this bill provides.

Mr. **Goldsborough.** Might I make a suggestion there?

Mr. **Brougham.** Yes, sir.

Mr. **Goldsborough.** There is nothing in the bill which will provide for 100-percent reserves, except a natural evolutionary process. There is no provision in the bill for a 100-percent reserve at all, but it is presumed that in the course of time, as these discounts are used, that the reserves of the banks would have to be increased and ultimately we would have 100-percent reserves.

Mr. **Brougham.** Yes; I understand that.

Mr. **Goldsborough.** It is a process of evolution rather than creating 100-percent reserves.

Mr. **Brougham.** Yes. The point that I want to make is merely that if the intent of this bill is carried out, and if the Government injects into our monetary and business system hundreds of millions, probably billions, of dollars, so long as the private banking groups of this country have also the ability to inject newly manufactured credits into the system, they will take advantage of that opportunity in which business is resuming operations at approximately capacity and the wants of the people are being filled by a method which I regard as admirable, and sound values will be increased in the underlying securities of the country, and the stock market will go up, and everybody will know that it will go up, and the banks will take that opportunity to lend to men who are speculators, and who will send the market up much faster than is warranted.

I believe that if we have here two means, two main means of regulating the credits for this Nation, especially when dollars are being provided by the Government, it is of very great importance that there should be a stop put upon 14,500 private mints, minting credit and injecting it into the system. That is the important thing.

I quite agree with Mr. Goldsborough that ultimately by the terms of this bill the Nation will be supplied with cash credits that are not born of debt, and the condition of whose existence is not debt, and that there will be less and less need of borrowing money, and that the banks will be supplied with these cash credits, their reserves will be increased, and we will have what should be a normal condition—that is, business normally being conducted on working capital of its own—provided by an increase in business and the profits that accrue from the increase of business up to the capacity of business to supply this country.

I should not object to having this bill passed just as it is without one line changed, and it would be a godsend to this country, but we have the record; when values are increasing, when business is increasing, the effect is felt in the stock market and the real-estate market, and those inflations we would have to avoid.

For that reason I would suggest that the title of this bill, the general descriptive title, be amended to read, after the words "of the country's power to produce"—"to abolish the practice of creating demand bank deposits by private groups upon fractional reserves, and for other purposes."

I have another amendment, which is to line 24, page 5, section 6 (a), after the words "of this act", which reads:

> Retailers, wholesalers, manufacturers, and prime producers are hereby authorized to make voluntary contracts with the Secretary of the Treasury under agencies authorized by law, or under the regulations of their respective trade and professional associations (1) in the case of retailers, in order to qualify them to dispense the retail discount and reap the benefit thereof; and (2) in the case of wholesalers, manufacturers, and prime producers, in order to qualify them to dispense their goods and services to qualified retailers, sharing with them the benefits of increased trade under said regulations or agencies. Said contracts shall specify in each case that the contractor agrees to such regulations as to cost accounting, maximum rate of profit on turn-over of sales, fair-trade practices, and professional ethics as shall be arrived at by negotiation between said contractor or trade or professional association with the Secretary of the Treasury, or other agency or agencies authorized by law. In the case of retailers, said contracts shall provide in each instance, that the retailer agrees to deal only with wholesalers, manufacturers, prime producers, and purveyors of services, to the extent that they are able to fill his orders, who shall have entered into contract, as aforesaid, with the Secretary of the Treasury.

That is the main amendment. I think it would be a pity if this bill did not take advantage of its voluntary contract nature and of the inducement for business to enter into these voluntary contracts without requiring those who have the great benefit to dispense this discount of price, to agree to a maximum rate of return on turnover of their sales. These new credits that are injected into the system at the point where the goods of the Nation are ultimately paid for we think should cause businessmen to agree, according to whether they are big or small businesses, largely through their trade associations—agree to a maximum rate of return, and make it perfectly reasonable and generous, if you please, but a maximum rate of return on the sales which they make.

Now, the packing companies of Chicago, for many years boasted that they got a rate of return on their sales of a fraction of 1 percent. A corner grocerman has to make perhaps 25 percent gross on turnover, or perhaps more; I do not know; but, at any rate, a great deal more than the beef trust, so-called, has made. If a concern is doing a national business, it should be restricted to a very small fraction of return upon its sales, and by the opportunity of this bill, if it should be reported by your committee to Congress (and supposing that Congress should pass it under the stress of conditions which I believe will become accentuated in the near future), we would have here an alternative to the exactions of the antitrust law—which thy have gotten around for many years—by voluntary contracts, whereby the big national manufacurers and sales organizations would by amicable settlement of these contracts agree to a maximum return on their sales, and the small dealers through their associations or individually would come also to an amicable arrangement.

It would not mean that they would exact that maximum rate. They would exact what they could under competitive conditions, but at any rate we have a problem here which the enactment of this bill, without this requirement, would bring immediately into——

Mr. **Goldsborough.** Mr. Brougham, just one moment there, if you do not mind.

It seems to me that the principle that you are now discussing is separate and distinct from the issue contained in the bill, and I am wondering if it has any place in legislation of this kind. Of course, we all know that this bill as it is now would not bring any Utopia; it would not interfere with the natural selfishness of mankind, but it is being discussed as a possible measure of relieving one particular difficulty, which is the ability of consumers to take up all of the wanted goods and services that our people are ready to produce.

So I am wondering whether what you have in mind has any direct relation to the bill.

Mr. **Brougham**. Yes, sir; because it concerns the central idea of price . The central idea of this bill, as I take it, is to lower prices to consumers.

Mr. **Goldsborough**. You do not mind my interjecting?

Mr. **Brougham**. Not at all.

Mr. **Goldsborough**. That would be a result, and a very happy result, I hope, but that is not the principle involved in the bill.

Mr. **Brougham**. Well, to increase the purchasing power, which is the same thing.

Mr. **Goldsborough**. The principle involved in the bill is the absorption by the people of all that the people can produce.

Mr. **Brougham**. Yes; and implicit in that, and welded in with it, is this prime question of price. You attack it by lowering the price level immediately to consumers, by giving a percentage which would increase their purchasing power, according to the terms of this bill, immediately by 20 percent.

Mr. **Goldsborough**. The discount would be 15 percent.

Mr. **Brougham**. But a 15-percent discount would be a 20-percent increase in purchasing power.

Unless you license also the basic producers of this country, who purvey to the retailers, what is to prevent their maintaining their present rigid price level, which many Government studies have shown has been very far above the average price level of commodities?

Mr. **Goldsborough**. I think that the answer to that would be this, that under this bill, if enacted into law, the consumer would not know anything about the discount. He might know what the general law was, but when he made a purchase, he would simply know that he was in better circumstances, and that his income was going further than it had before.

Now, the question that is disturbing you, as I understand it, is whether or not chiselers of various kinds could take advantage of that situation and would try to maintain their prices and get the advantage of the discount also.

Mr. **Brougham**. No; I mean the basic commodity industries that have held their price levels rigid at the expense of production and sales all through the recent depression, and they are doing it again, despite the fact that the steel company only yesterday reduced by five and a fraction percent one of its——

Mr. **Goldsborough**. That is not the problem that we are attacking in this bill. As to the problem of price-fixing, and the problem of restricted production, there is no attempt to attack them in this bill. This is only an attempt to do what I said a while ago, to bring together consumption and production in this country. Of course, there other difficulties of which you speak should be treated, but it is not the objective of this bill to treat them at all.

Mr. Brougham. I think it is. Of course, the objective of this bill is to increase the purchasing power of consumers, no matter what the prices are of basic commodities, and to a considerable degree it will do so.

Mr. Goldsborough. That is true; but what I have reference to is this, that we have on the statute books now, laws in which we attempt to attack the very problem you are discussing this morning. We have proposed legislation on that coming before us all the time, because the problem is always an immediate problem, but what we are trying to do in this particular bill, and I will attempt to state it in another way in order to clarify it in your mind, is to have a continued action which will supplement buying power whenever it is needed, so that in case of an incipient depression, you would always have this cushion which would guarantee such a lowering of prices as to make buying power continuous and therefore stimulate production and manufacturing and everything else.

That is the specific purpose of this measure.

Mr. Brougham. Yes, sir; but you are providing here with this, and in fulfillment of that purpose, a new framework, a new economic framework, with its special set of problems, one of which would be an attempt on the part of these producers immediately to raise their rigid price structure still more, in order to take what the President calls the cream off of the prosperity which you will produce by the effect of this bill.

Mr. Goldsborough. The only way that you could attack that is by destroying monopoly, which is not the purpose of this particular bill.

Mr. Brougham. The purpose of this amendment is not to destroy monopoly—that is, not to destroy what they call concerted price fixing. I think some distinctions are made between that and monopoly, but to control it in such a way that it will have a roof.

Mr. Goldsborough. Of course, my own opinion is this, that what will happen, I have no doubt, is that some retailers will begin chiseling——

Mr. Brougham. I am not afraid of the retailers.

Mr. Goldsborough. Just a minute. I am coming to that. When they do that, they will immediately get in trouble with the authorities and their license will be taken away from them, and they will not be able to compete with other retailers and they will be put out of business because they cannot get their license back. That would be an immediate warning to all of the other processors that they had better keep their noses clean.

Mr. Brougham. Yes.

Mr. Goldsborough. You cannot attempt, it seems to me, in one bill to cover all of the ills of mankind, and it is not the purpose of this bill to do that.

Mr. Brougham. You cannot; and it may be that we should take up the necessities as they arise, but I am suggesting this as a rounded picture.

The Chairman. You are a man who certainly will understand the difficulties in doing something that is new in this field of legislation.

Mr. Brougham. The method of voluntary contract is not new.

The Chairman. But the machinery of this bill is new, and what Mr. Goldsborough had in mind is that if you attempt to kill too many snakes at the same time, you will not get anywhere.

Let me make this suggestion, that you discuss this particular bill, and let us have your views on it, because the committee would love to have them and you could probably be of help to us, and if you have any suggestions that you want to make, we would be glad to have them.

Mr. BROUGHAM. I will hand to the stenographer my request for amendments, in order that it may be made a part of the record——

The CHAIRMAN. That may be done, without objection.

(The amendments submitted by the witness are as follows:)

Amend by insertion of italicized matter, at the fifth line of the descriptive title of the bill:

"* * * of the country's power to produce; to abolish the practice of creating demand bank deposits by private groups upon fractional reserves, and for other purposes."

Amend by insertion at page 5, line 24, section 6 (a), after the words "of this Act":

"Retailers, wholesalers, manufacturers, and prime producers are hereby authorized to make voluntary contracts with the Secretary of the Treasury under agencies authorized by law, or under the regulations of their respective trade and professional associations (1) in the case of retailers, in order to qualify them to dispense the retail discount and reap the benefit thereof; and (2) in the case of wholesalers, manufacturers, and prime producers, in order to qualify them to dispense their goods and services to qualified retailers, sharing with them the benefits of increased trade under said regulations or agencies. Said contracts shall specify in each case that the contractor agrees to such regulations as to cost accounting, maximum rate of profit on turn-over of sales, fair-trade practices, and professional ethics as shall be arrived at by negotiation between said contractor or trade or professional association with the Secretary of the Treasury, or other agency or agencies authorized by law. In the case of retailers, said contracts shall provide, in each instance, that the retailer agrees to deal only with wholesalers, manufacturers, prime producers, and purveyors of services, to the extent that they are able to fill his orders, who shall have entered into contract, as aforesaid, with the Secretary of the Treasury."

Amend, at lines 5 and 6, on page 13, section 301 (b), by striking out the words "revolving fund" and inserting italicized words to read:

"* * * of like nature which may be provided shall constitute *the basis for issuance of corresponding sums of demand bank deposit currency* for the stabilization * * *."

Amend on page 14 by striking out all of paragraph (f), after line 8, and on pages 14 and 15, by striking out all of paragraphs (g) and (h) and substituting the following sections:

"DECLARATION OF POLICY

"SEC. 302. It is the intent of this act that the National Credit Control Account in all banks shall be maintained in approximate balance at all times.

"It is the intent of this act to control the volume of the means of payment for goods and services in harmony with the ability of the whole Nation to produce and consume them on a rising standard of living, so that excess expansion of money and a consequent undue advance in the price level shall not occur, and that the present system of issuing money through private initiative for profit, resulting in recurrent disastrous inflations and deflations, shall cease.

"To such end the privilege of the commercial banking system to make loans and issue deposits against them on the basis of fractional reserves is hereby rescinded. The right of the banks to loan the means of payment shall be limited to the amount of primary deposits in their possession and their own resources. Such loans shall be for account of the depositors, and shall be charged against the balances of said depositors and credited to the borrowers. The banks shall act solely as agents in the loaning of customers' deposits, and shall receive therefor a commission for collection of interest, the amount of which shall be fixed by the National Credit Commission, but not in excess of 10 percent of interest return upon such loans: *Provided*, That upon the authority of the National Credit Commission, the banks may, at their discretion, allow interest, not exceeding 1 percent per annum, to time-deposit customers whose funds they have been unable to loan or who desire to retain their deposits unemployed. The responsibility of the banks to their customers under this provision shall be the same as now obtains in the existing system of 'loans for account of others.'

"The privilege of the banks to rediscount commercial paper and borrow upon Government securities at the Federal Reserve banks shall be limited to collateral actually owned by them. Collateral security conveyed to them as agents for depositors for whom they have negotiated loans, shall be held in trust for account of such depositors during the life of the loan.

"Depositors who have authorized the loaning of their deposits shall give sufficient notice to the bank of their desire to withdraw such funds. The banks may transfer any loan from one depositor to another, at the same time transferring the collateral in trust, rather than having recourse to calling in the loan and reissuing it.

"A bank shall be entitled to charge a commission to the borrower for negotiating loans not exceeding 1 per centum of the face value of the loan.

"BANK DEPOSITS PAYABLE IN LEGAL TENDER CURRENCY

"SEC. 303. It is hereby enacted that the Comptroller of the Currency shall at all times be prepared to meet the requirements of the banks for such currency, legal tender for all debts, public and private, as may be called for withdrawal from them by their customers.

"Transfer of collateral to offset the drafts of currency so demanded shall not be required of the banks. The privilege of creating deposits upon a fractional basis of reserves having been withdrawn from the banks in the interest of sound national money, it becomes the responsibility of the National Government to see that the primary bank deposits already brought into existence under the existing system can be validated.

"The banks shall return all currency that has been withdrawn for validation of deposits to the Comptroller when redeposited, excepting only such working reserves of normally circulating currency as may be required. Nothing in this Act shall be interpreted as releasing the banks from obligations they have already incurred to the United States Treasury or Federal Reserve banks for currency now in their possession.

"The banks shall furnish a strict accounting of the currency called for by their customers in excess of normal requirements of business, such as might occur in time of financial stress.

"The banks shall act simply as agents of the Comptroller of the Currency in validating bank-deposit money with legal-tender currency, and no charge therefor shall be made upon either side for such service.

"SEC. 307. Improper use of the certificates herein provided to be issued shall be a misdemeanor and shall be punished by a fine of not exceeding $10,000 and imprisonment for not exceeding five years."

Mr. BROUGHAM. I will now proceed to give my views on this bill in toto.

The CHAIRMAN. All of us agree that the purposes which Mr. Goldsborough has in mind are desirable. There is no argument about that, but there is a failure, first, to understand this bill fully, and then the criticism is lodged, by those who seem to oppose it, that it is unworkable.

Mr. BROUGHAM. I should like to state that it is workable by the experience of the businessmen of this country; that it is only extending what big business of this country has already accomplished by individual aggregations of capital; that the attempt of this bill is fundamentally to take advantage of the economies of a full-capacity production of the industries of this country in order to lower the price level to consumers——

The CHAIRMAN. How about the farmer?

Mr. BROUGHAM. Also to take care of the capacity production of the farm, of everything in and above the ground that is produced, and to lower the price level to the consumers on those realized economies.

I say that that has been proved by the businessmen of this country. They have again and again proved that they could sell their products below cost for a time, in order to take advantage of a larger volume of demand, and step up into that larger volume of demand and, through economies of larger-scale production, still sell at that lowered price and make a profit. That is the heart and kernel of this bill, as I have worked it out.

It would be quite possible for manufacturers now, those who have been gathering here in Washington during the last few weeks, to get together and duplicate this system which Mr. Goldsborough proposes through common agreement among themselves and on their own books as businessmen, and I have worked out a memorandum to that effect; they could combine together to produce at capacity for wanted goods and services, form a well-rounded aggregation of producers—prime producers, manufacturers, retailers, wholesalers—and agree upon an initial discount upon price, and all down the line, and provide a system of trade credits backed up by trade-credit warrants on their own books, and do precisely the thing that Mr. Goldsborough proposes in this bill.

Mr. CRAWFORD. Would that keep it entirely out of the banking field?

Mr. BROUGHAM. It would keep it entirely out of the banking field. It would result in their not having to go to the banks for added accommodations, and they would do it upon these economies which they would anticipate and realize, just as it has been done by individual enterprisers. Of course, you will say that there has been a great mortality, a greater mortality among manufacturers that have attempted this individually than there have been survivors, but on a common insurance basis of manufacturers and producers of this country, and of the retailers, they could get together and do precisely the thing that is proposed in this bill, and they could establish these circulating trade credits, allowing them as compensation to the retailers in the cooperative organizations, in the sum of the percentage of their discount upon prices to consumers, those trade and credit warrants could be passed back by the wholesalers to manufacturers in increased volume of orders as a discount upon wholesale prices, and could circulate around, and they could be paid to their workmen, and the workmen could use these trade-credit warrants exactly as though they were cash, and take advantage of the discount.

Now, I worked this out in some detail, because it furnishes an interesting sidelight upon what Mr. Goldsborough is driving at here through a reform of the currency system.

This reform of the currency system, I think, is the solution, if Congress will act, because it will end the private manufacture of credit and its induction into the money system primarily, initially, as debt to these private groups. Such debt-making is not according to my theory of the proper way in which money should be born. It should be born as a requirement to balance added productive capacity, and should be based upon whatever price level is determined upon, perhaps the existing price level, for that added capacity, as though it were actually being utilized to pour the commodities into the hands of the consumers.

Of course, early in the history of this country, they had a few millions of money, and now we have billions. We need a certain quantity of money, and we have found quite certainly that it turns over as consumer income within certain limits, so that the velocity side of it is not of so much concern. If we have a permanent addition to the production of this country, we should have a permanent addition to the amount of money with which to exchange it, and that should cost no more than the tickets for an additional thousand seats in a theater, namely the cost of printing. It belongs already to the people, because its value is inherent in the values which they have produced and in the productive capacity which they have produced, and it should be given to the people, since the money, which has no value in itself, acquires its value only as an exchange value of goods which belonged to them initially, and should not be created as a debt which they would have to pay to private groups of individuals who arrogate this power of manufacturing the money to themselves.

Mr. **Gifford.** Who pays for those tickets?

Mr. **Brougham.** The theater owner, and he goes to the printer of tickets and says, "I want to print 1,000 additional tickets." If the printer should say, "I belong to an association of printers that have a monopoly on this, and I will charge you not only for the printing of these tickets, but whatever is entered on the face of these tickets, $1 or $3.50, and you will have to pay that before you can have these tickets," there you would have an exact parallel with the modern money system, which says to anybody if they want any new money that they will have to pay initially for the cost of producing, and in addition pay according as that money is denominated——

Mr. **Gifford.** Who is going to hold the bag in the last instance?

Mr. **Brougham.** The people of the United States will hold the bag, in their capacity to produce.

Mr. **Gifford.** The Government?

Mr. **Brougham.** With the Government as their representative.

This bill is a bill to increase private property in this country, to increase the ability of people to acquire it, to use their own power, to reemploy them, to keep property values stable, to prevent what has happened in the last few months, when property values have diminished by billions, through withdrawals of the medium of exchange, and so long as we have private groups issuing this medium of exchange, they can withdraw it, and they do withdraw it.

When the 100 largest banks of this country last year disposed of their holdings of Government bonds, they withdrew 2 billions of money that was being used in trade in the large, populated centers of this country, and I think that there is a direct correlation between that and the fact that in New York, the richest State in this Union, one in six is either on relief or is on rolls of the W. P. A.

Mr. **Transue.** Is there a connection between the selling of those Government bonds and the raising of the Federal Reserve requirements?

Mr. **Brougham.** That, together with the raising of the reserve requirements, was a signal to those who held stocks to dispose of their stocks, and last spring and summer they were doing it quietly, and, knowing that the stock market would go still lower, they held the money which they took out of business by disposal of the stocks in idle, hoarded accounts.

Mr. **Transue.** You say "they." For my own part, I would like to know whom you are talking about.

Mr. **Brougham**. The rich holders of stocks, when this selling movement began.

Mr. **Transue**. Isn't that pretty largely all of those people in the United States who invested in stocks?

Mr. **Brougham**. Why, certainly. It became irresistible. They had to sell when the market was in that situation, and I am not blaming anybody, but the point is that once they sold those stocks, they did not invest the money which they received for them, because it was a time of falling prices, and prices have fallen faster, and business has receded much more speedily than in any other previous time in our history, and why should I, who have sold my stocks, invest my money, knowing that the bottom is dropping out of the market?

Mr. **Luce**. What can they do with their money?

Mr. **Brougham**. Idle demand deposits were growing, and——

Mr. **Luce**. That is not an answer to my question, which is: What did the man who sold that stock do with his money?

Mr. **Brougham**. He put it in the bank.

Mr. **Luce**. What did the bank do with it?

Mr. **Brougham**. It is largely held on demand, Mr. Luce. It is suspended. It is hoarded deposits, very largely.

Mr. **Luce**. It is in the banks.

Mr. **Brougham**. The banks cannot invest it. Beyond a certain extent banks are not investors.

Mr. **Luce**. But the banks have that money.

Mr. **Brougham**. Yes.

Mr. **Luce**. Do you know of any specific instance in which a man with good credit, character, and so forth, was unable to borrow that money?

Mr. **Brougham**. Where he is unable to borrow that money?

Mr. **Luce**. Yes.

Mr. **Brougham**. Well, if he has sufficient collateral on the declining market, he can get that money, but that collateral is declining in value all the time, and it means that a man with the utmost probity finds that his collateral is now insufficient to borrow.

Mr. **Transue**. Will you just follow this through with me? We will take, for instance, when the stocks, we will say of General Motors, wore down, and they were selling these stocks that you speak of, and when they went to what they were last spring, did that help in creating employment and all of the other things, and in taking up the slack?

Mr. **Brougham**. Possibly, to a certain extent, but let us take the record in 1929, when the stock market went up quite a bit, and then afterwards it went down, down, down. Now, I get from Professor Fisher weekly his index of wholesale prices. I find that it rises two-tenths of 1 percent in a week, and then that it goes down six-tenths of 1 percent. The general trend is downward, and the general trend of the stock market is downward, so long as we have this stagnation of business and this lowering of the general price level.

Mr. **Transue**. Lowering of the general price level? What are you talking about?

Mr. **Brougham**. The average prices of all commodities.

Mr. **Transue**. Take the man who walks into a store and wants to buy something——

Mr. **Brougham**. I am referring to the average.

Mr. **Transue**. Of consumers' goods?

Mr. **Brougham**. It will be on consumers' goods, and if it is not already, it soon will be, and we will find a marked decline in the price level, in the cost of living, of the retail price level. That follows with a lag after a violent decline of the wholesale price level, and that violent decline of the wholesale price level we are having now, and it has persisted now for about 5 months. We have had a recession of business six times as fast as during the first 2 years of the previous depression, and there is a school of thought which is born of a hope that there will be a rebound just as rapidly. Well, there will be, if it is managed so, but there won't be through Mr. Luce's reliance upon businessmen of property borrowing at a time when they do not want to borrow.

Mr. **Transue**. But the point that I am interested in is this: When the prices go down on consumers' goods, it seems to me that that would make it easier for those who have some purchasing power to go in and get more consumers' goods, and consequently puts more people to work, and start the thing going the other way.

Mr. **Brougham**. Unfortunately, the process that takes place is too violent for that. Men are thrown out of employment so rapidly that the purchasing power of the consumer declines much faster than the cost of living declines, so that we are now in a tail spin just exactly as we were in October 1929 and in the years following that.

Mr. **Crawford**. Is it not also true that as the price level on all commodities such as cotton, wool, mohair, and hides declines, and it moves on into the finished product, on the retailer's counter, that that very decline tends to cause the fellow who still has some buying power left to defer the date of purchase, anticipating that his dollar will buy more than it did previously, except in those cases of sheer necessity?

Mr. **Brougham**. That is true.

Mr. **Crawford**. And that those purchases thus stimulated by the drop in price are just a little atom compared to what would be purchased if the whole credit of the people was buying and consuming?

Mr. **Brougham**. Yes.

Mr. **Luce**. Everything that has been said I accept freely, but I do not understand why, when the banks have the money and can only make a profit by lending the money, you should lay the responsibility for this situation on the banks.

Mr. **Brougham**. I have not any quarrel with any individual banker.

Mr. **Luce**. One moment. Why, in those circumstances, should there be agitation here in Congress to create more money?

Mr. **Brougham**. The reason for that agitation here in Congress was given by the Honorable Robert L. Owen in the first hearing on this bill, or upon its predecessor, in which he showed the intense concentration of bank money in the hands of relatively few depositors in this country.

Mr. **Luce**. That does not interest me, sir. I am interested in my own bank, in my home town.

Mr. **Brougham**. He showed that the business of this country was being done on demand deposits not exceeding 3 billions of dollars.

Mr. Luce. But you are not following me, sir. I want to know why, when the Waltham National Bank, which so far as I know has no connection with any of these big banks, has plenty of money to lend, and when the tool makers, and we make fine tools there, are unwilling to borrow, you should lay the blame on the bank.

Mr. Brougham. I do not.

Mr. Luce. Why should you say that there should be more money, when the banks have more money than they can lend now?

Mr. Brougham. There should be more money, but it should not be in the banks.

Mr. Luce. How did it get into the banks? No man carried it around in his purse.

Mr. Brougham. There should not be any more debt money. I am against the increase in debt money, and any greater aggregations of debt money. I do not believe that we ought to borrow in a time like this.

Mr. Luce. Now, you and I are in perfect agreement, but you have not told me why you want the bank to have more money, when it already has more than it can lend.

Mr. Brougham. I do not blame the banks or the bankers, and I wish that we might get out of the personal end of it.

Mr. Luce. You are the only man around here that does not blame the banks.

Mr. Crawford. I just want to make this observation, that the gentleman very distinctly said in his original statement that it ought not to be blamed on the banks, but that the man who might be able to make a loan was not willing to go to the bank and ask for it, and he pointed out that that was the trouble.

Mr. Brougham. The only way that debt-free money can get into existence is in some such way as Mr. Goldsborough proposes. At present we have a system of banking against which I have an indictment, which allows the Nation to have money only at the price of initial debt upon its creation, and that I believe is a very serious defect in our system, where we have ample resources, where we have men and materials and inventions, and the most modern equipment, and have everything except debt-free money.

Mr. Transue. How does that compare with what the other countries have, in the way of creating money?

Mr. Brougham. It is identical. It is a world-wide defect, and that is the reason why these depressions are world wide. We have one period in which this debt money is let out, and then when prices have gone up and men are employed, it is recalled by these private individuals who refuse to reissue it at the behest of their own stockholders and for their own profit and benefit, against the public welfare, and we are in that period now.

Mr. Luce. But, my dear Mr. Brougham, the bank that I am speaking of is not unwilling to lend.

Mr. Brougham. Not unwilling to lend, but I am unwilling to have it lend.

Mr. Luce. But now we get off to another question. I want to pin you down to this one thing. I cannot understand why gentlemen come here, as the gentleman yesterday, with a proposal to entice, induce, or otherwise get the banks to lend more money.

Mr. **Brougham.** Well, the poultry men have a name for it. They call it cramming, and they fatten their fowls that way. I am not for it at all. I am not for any increase in debt in this country, and I feel that Mr. Goldsborough is not. He wants to increase the amount of cash-credits in the accounts of the men who are out to make profits, and to do it in a legitimate way. Whenever a banker creates money, it costs him no more than the writing of a check would cost, and the trouble is that he obligates himself for a great deal more than he should, and that is what makes banking the risky business that it is. I do not know of any sound businessman who would do what a banker does, contract for more obligations than he has assets for, but the banker does that regularly, and that is just not sound business.

Mr. **Luce.** Do you think that character is not an asset?

Mr. **Brougham.** Oh, character is an asset, and all that, and in good times a splendid asset.

Mr. **Luce.** The businessman borrows on the strength of his character.

Mr. **Brougham.** But in bad times character is not a good asset, if you have not got something else.

Mr. **Transue.** If the depositors come in and want their money, and all that the bank has are notes based on character, they do not pay those deposits.

Mr. **Brougham.** They do not pay those deposits, and we have here something that concerns the Bank of Waltham only as it concerns every bank in the United States. They cannot lend on character today.

Mr. **Transue.** I want to get back to the question that Mr. Crawford raised, as to the way people buy. He said that if the market was falling, people will want to wait for falling prices before they make purchases. I have had the belief that if the people of this country had money to pay for the necessities of life, and they would go and buy those things, and that that would start things going again.

How yould your plan get to those people who have not had the money with which to buy originally?

Mr. **Brougham.** You would find that that situation would mend itself in a few months' time. It would help those people indirectly, but immediately by the fact that their relatives who have a given purchasing power find it increased by 20 percent, and they could get that 20 percent, perhaps borrow it from their relatives; the relatives would be able to help them so much the more, and as this new volume of demand came in to the retailers, the orders would go back in increased volume to the wholesalers, and then to the manufacturers, and the manufacturers would find that they have to take on new men in employment, and in a few months' time, if you have this 15-percent discount in price to consumers, you would find that business was going ahead at larger and larger capacity, and that the thing would be managing itself.

Mr. **Transue.** Right along that line, in the New York Times of last Sunday, they had a statement showing that corporations made more money, according to their reports, last year than they had made during 1936, by 16 percent.

Mr. **Brougham.** During the last quarter of 1937?

Mr. **Transue**. It gave the reports for the year, and also showed that in 1936 they made more than they did in 1935. So it seems to me that we have had all of the unemployment in the last quarter of 1937 and the beginning of 1938.

Mr. **Brougham**. During the last quarter it has increased rapidly, and during the next quarter it will increase still more rapidly and business, seeing that things are folding up, will continue throwing men out of employment. Of course, they must. It does not depend upon the profit made during the first three quarters. Just as soon as the bottom drops out of the market, men are thrown out of employment.

Mr. **Transue**. Then, too—and whether there is any significance in it or not, I do not know, but the number of automobiles of one company sold to consumers in the United States was far greater by thousands of cars than the number that they are producing at the present time. Does that indicate any trend to you, as far as the corporations are concerned?

Mr. **Brougham**. If that were so in the automobile industry generally, I should regard it as a most hopeful sign.

Mr. **Transue**. That was in the New York Times of yesterday.

Mr. **Brougham**. There must be special reasons for that increase in the sales of that particular car. As a matter of fact, the automobile industry is in the doldrums.

Mr. **Transue**. I am just calling your attention to the fact that the number of cars that they sold to consumers in January was 8,000 to 10,000 more than the number that they made during January.

Mr. **Brougham**. I wish that you could argue from that particular case that there is any hope for the general situation.

Mr. **Crawford**. Are those all new cars?

Mr. **Transue**. I cannot say as to that.

Mr. **Crawford**. Will the gentleman yield?

Mr. **Transue**. Yes.

Mr. **Crawford**. One of the automobile manufacturers in my home State told me that during the week between Christmas and New Year, his firm had 80,000 complete new cars in storage, awaiting the market.

Now, let us assume that his sales run 20,000 a month. He can run for 4 months selling 20,000 cars each month in excess of his production and still be even at the end of the 4 months' period.

Only last night I spent 5 hours with seven manufacturers here in this city—they do not operate here but they were in the city—and I understand from them that manufacturers are leaving their places of business in charge of their lieutenants, or their assistants, and going away on trips where they can change the atmosphere and get away from their desks for a while and somewhat clear up their minds, with the factories shutting down and inventories being unloaded as best they can under the conditions which govern, and you cannot blame a man for doing that. The man in the bank has to keep in mind the fact that during the next 3, 6, 9, 12, or 18 months his demand depositors may come to the window and call for their money, and he wants to be liquid when they come.

The man at the head of a business has to keep in mind that he is trying to preserve the capital structure for his stockholders; and if he proceeds to cram warehouses in excess of his sales on a declining market, he certainly is headed for trouble; and if he is not careful on that kind of a program, the banks will call his loan, if he has any.

Mr. **Brougham**. That is my objection to Mr. Cromwell's inducement loans.

Mr. **Transue**. That being so, what is the reason why these automobiles are piling up, or other goods, if they are producing more than they can sell currently, when you have a lot of people needing those very things, and why is it that the market is drying up? That is the question that we have to get at. Is it because those things are too high-priced?

Mr. **Crawford**. I personally think that has a lot to do with it. They are too high-priced because we put too many things into the cost formula, and we put more in every day.

Mr. **Gifford**. I had a very beautiful automobile, costing a lot of money, listed at $4,600. They allowed me $150 because it was old, but it was in perfect condition. Whoever gets it will have a wonderful automobile, but the second-hand cars have been selling at any price, and the country is simply filled up with them.

Mr. **Williams**. Isn't it also a fact that right at the time when they were in high production and they were producing at less cost than they ever did they raised the price?

Mr. **Brougham**. That is what the railroads are trying to do.

Mr. **Williams**. Isn't that a fact—that that is what happened in the automobile business last summer?

Mr. **Brougham**. Before the Interstate Commerce Commission, the railroads want to raise their rates.

Mr. **Williams**. I am talking about the automobile business. That is a fact, as I understand it.

Mr. **Brougham**. Well, I do not know how to explain it.

Mr. **Williams**. Of course, that raising began about September of last year, and it began at a time when the country apparently was engaged in a very high productive capacity, higher than it had been at any time since 1929.

Now, what was the cause of that?

Mr. **Brougham**. They were at a higher level of costs than the present market can now absorb, and that is the reason that industries will hold up their prices by collusion.

Then they had to pay on a higher cost level for their raw materials on their important products; and in order to get any profit at all, they had to hold up the prices of the finished goods.

Mr. **Williams**. And is it not also a fact that at that very time they were making very substantial profits and there has been a recession since then but at that time it was the highest?

Mr. **Brougham**. There is a tendency when the market narrows——

Mr. **Williams**. But what was the cause of the market narrowing under those conditions?

Mr. **Brougham**. The cause of the market narrowing was the withdrawal of money from business.

Mr. **Williams**. What was the occasion for the withdrawing of money when business at that time was making unusually good profits?

Mr. **Brougham**. It was the tightening of money by the bankers who could not meet the Reserve requirements otherwise without calling in their loans and not reissuing them, and the declension of the stock market, which required those who sold their stocks to hold their receipts for reinvestment.

Mr. **Williams**. How much did the banks have to call in in order to meet the reserve requirements of the Federal Reserve bank?

Mr. **Brougham**. I do not know.

Mr. **Williams**. Then why do you make the statement that that was the cause of it? The fact is that it was only a comparatively small amount.

Mr. **Brougham**. Whatever it was, it was so much——

Mr. **Williams**. But it was so small it did not amount to anything.

Mr. **Brougham**. By the disposal of Government bonds, by the banks recalling all of that money from business——

Mr. **Goldsborough**. Pardon me, Mr. Brougham, but some of the members want to get away, I know that I do. Could you come back here next Tuesday?

Mr. **Brougham**. I think that I could.

Mr. **Goldsborough**. Then we will meet again next Tuesday morning.

(Thereupon, at 12 o'clock noon, an adjournment was taken until Tuesday morning, February 15, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

TUESDAY, FEBRUARY 15, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on H. R. 7188 were resumed at 11:02 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Evans, Mr. Transue, Mr. Luce, and Mr. Crawford.

The **Chairman.** The committee will be in order, please.

Mr. Brougham, you may resume your statement.

STATEMENT OF HERBERT BRUCE BROUGHAM—Resumed

Mr. **Brougham.** Mr. Chairman and gentlemen, I prepared last month a memorandum for Major Angas, the international financial expert and market forecaster, on the subject of Pump Priming by the Government. It bears directly on this bill, and with your permission I should like to read it to the committee. It is a short memorandum.

The **Chairman.** Yes.

Mr. **Brougham.** It reads:

> Before accepting the monetary solution outlined by Dr. Gardiner C. Means (S. Doc. 13, 74th Cong., 1935) I would urge consideration of the pump priming by the Government from 1933 to 1937, with precisely this end in view.
>
> The pump-priming theory contends that stimulating the spending of new money, manufactured by the banks and lent to the Government, results not only in primary but also in secondary increases in income and employment. That is, there is a net turn-over of the same new money as income in consumers' pockets, under normal conditions, about three times a year.
>
> ### DEFECT OF PUMP PRIMING
>
> It is true that the upswing that culminated in August last was not initiated by anticipating private investments. Public spending did fill this gap with its primary and secondary increases in income.
>
> But the pump-priming theory also contends that after a certain period deficit spending can be stopped, either by curtailing public expenditures or by increasing taxes, without danger of a new recession.
>
> What, actually, has happened?
>
> The stimulating expenditures came to a peak in the second half of 1934, and then declined somewhat until 1937, when they fell rapidly; while nominal income and employment further increased.
>
> Thus diminution in stimulating expenditures did not result in new recession until August 1937, when it was combined, indeed, with other factors.

Yet during 1937 there was radical curtailment of deficit expenditures by $3,000,000,000. That factor alone might have produced the recession.

Of course there were the other factors which I mentioned at the last hearing.

Certainly there was delay in the expected tertiary effects, which, in relation to existing idle capacities, were not large enough, through stimulating expenditures, to lift the consumers' purchasing power up to the point where increased demand made new investments unavoidable, thereby overcoming even psychological hindrances.

Recently, but too late, it appears, the administration has committed itself to a more permanent public policy of stimulating investments—represented in housing projects—in order to supplement the temporary policy of deficit spending.

It is too late because we now have the cutting weight, as of a guillotine, of the sharpest recession in our history before the housing projects could be brought into play; also, we have the fiscal burden ensuing from past public borrowing.

We must bear in mind, moreover, that throughout the pump-priming period—even at the height thereof—the net income turn-over of cash and demand bank deposits failed to recover the norm of three times annually; instead it stuck around two. That is, the total cash and credit on which trade and consumer purchasing power depend has throughout this period lost its efficiency by one-third.

Governor Eccles, you will remember, testified before your committee in 1935 that during the depression one-third of our money had disappeared through the recalling of loans and their nonreissuance.

During this Roosevelt period the money itself has lost in its efficiency in turn-over by one-third, so that while it has increased in the size of bank deposits subject to check, and increased somewhat in cash, it is really one-third less in terms of turn-over than the sum of cash and demand deposits in 1937.

DECLINE IN INCOME VELOCITY

Dr. Lauchlin Currie, Assistant Director of Research of the Federal Reserve Board, has made progressive studies of income velocity from 1921 to 1937, inclusive. Dr. Currie's figures of money—cash and demand bank deposits—in its annual turn-over as national income for those years follows:

Money and income velocity

[Amounts in millions of dollars; velocity in times per year]

	Money	Income produced (kuznets [1])	Income velocity
1921	21, 358	56, 488	2. 65
1922	21, 826	57, 355	2. 63
1923	23, 376	66, 738	2. 86
1924	23, 987	67, 370	2. 81
1925	25, 510	71, 792	2. 81
1926	26, 051	76, 207	2. 93
1927	26, 680	74, 036	2. 77
1928	26, 899	77, 271	2. 87
1929	27, 142	80, 484	2. 97
1930	26, 110	70, 664	2. 71
1931	24, 616	55, 769	2. 27
1932	20, 909	40, 622	1. 94
1933	20, 285	39, 636	1. 95
1934	23, 287	48, 700	2. 09
Department of Commerce:			
1934	23, 287	49, 575	2. 13
1935	26, 537	54, 956	2. 07
1936	31, 442	63, 799	2. 03
1937	32, 303	68, 000	2. 11

[1] After adjustment for treatment of income produced in Government service.

Note that during 1936 and 1937, when the income turnover of money had shrunk to 2.03 and 2.11, respectively, as compared with 2.97 in 1929, the actual cash and deposits of the Nation subject to check on demand had risen above the $27 billions of 1929, to $31.4 billions and $32.3 billions, respectively. We have here the phenomena of more ready money in the banks and a shrunken income for the consumers of the Nation in 1937, as compared with 1929.

By another approach to the same subject, Dr. Fritz Lehmann, of the New School for Social Research in New York, finds that the ratio of monthly bank debits to all deposits was 0.82 in June 1933, 0.68 in December 1933, 0.72 in June 1934, 0.69 in June 1935.

That is during the time of the greatest amount of pump priming.

Since time deposits are included in all deposits, and since in this period time deposits increased more slowly than demand deposits, Dr. Lehmann concludes that the "velocity of circulation of demand deposits must have declined."

CONCENTRATION OF DEMAND DEPOSITS

The reason for such decline in velocity of demand deposits as consumer income becomes apparent from a disclosure made when the Federal Deposit Insurance Corporation reported on the deposits in the banks of the United States in October 1934.

The Corporation found that in all the commercial banks of the United States there were $35,000,000,000 of deposits, $20,000,000,000 of which were above $5,000 each, and which were held by less than 2 percent of the depositors; and 98 percent of the deposits, consisting of 49,750,000 deposits—not depositors, but deposits, some people having one, two, or three deposits—it found that 98 percent of the deposits represented only $15,000,000,000; and of those $15,000,000,000, the record shows that about $11,000,000,000 were savings accounts, leaving about 49,000,000 deposits with less than $4,000,000,000, on which they could check for the transaction of the Nation's business.

A part of that $4,000,000,000 was time deposits, too, but the classification is not completely available as to the amount. It was not known how much of that $4,000,000,000 was time deposits, but about $1,000,000,000 represented certificates of deposit. It suffices to observe that 49,000,000 deposits had a reservoir of checking accounts of about $3,000,000,000 or less, whereas there had drifted into the hands of our great corporations as surplus reserves, in part—and that classification is not definitely known—$20,000,000,000, approximately, a very large part of which was subject to check.

Here is a measure of the inadequacy of purchasing power in the hands of the mass of consumers. It shows clearly, I think, the concentration of payments by the Government into relatively few hands during the "pump-priming" period, notwithstanding the payments for relief of unemployment through Mr. Hopkins' office. Of course, the net income turn-over into the hands of the masses of unemployed during this period was zero.

Since 1934 the situation in this regard has not improved, as income velocity has held at approximately twice the sum of cash and demand bank deposits per year, instead of rising to the normal of thrice for 1929 and preceding years, notwithstanding the increase of demand bank deposit totals.

METHOD OF "PUMP PRIMING" MUST BE CHANGED

The inference is plain. If we are to go back to more of the sort of "pump priming" that characterized the period 1933–37, with steadily mounting debt and taxes and great masses of workers still unemployed, the inadequacy of mass purchasing power will likely persist. In fact, it will grow should the flexible consumer group of prices be trained into line with the inflexible group of basic-materials prices.

That, you may remember, was the suggestion of Dr. Gardiner C. Means in his study of the inflexible groups of basic prices. This is true because wages always lag considerably behind a rise in the general price level.

So with the resumption of pump priming of the old order, the overladen economy may lift a little on the new swell, only to sink deeper into the new trough of depression.

THE NEEDED DEPARTURE

The way out, it seems to me, in view of the exacerbated situation, is strictly along two lines: (1) Issuance of national money or national credit, not borrowed but manufactured by the Government; and (2) application of the new money directly to an increase of mass purchasing power.

By acceptance of this dual policy the President would begin by availing himself of the power conferred upon him by the Thomas amendment, which permits an emergency issue of United States notes, or "greenbacks," or $3,000,000,000 to pay the extraordinary expenses of the Government and help balance the Budget.

Further, the President would ask Congress for power to issue more billions of United States notes, or an equivalent of debt-free credit, fully to balance the Budget during the current and the succeeding fiscal year.

In addition, he would ask for an issue of United States notes, or the equivalent in debt-free credit, equal to one-half the difference between $68,000,000,000 (estimated national income for 1937) and $90,000,000,000, set by the President as his minimum goal for the national income in 1938.

The issue of one-half such difference of $22,000,000,000—his goal of new and attainable national income this year—or $11,000,000,000 of new cash or equivalent debt-free credit, would be on the assumption that within a year or a year and a half, as paid out, the new money would turn over as new income twice net per annum to achieve such minimum goal. Quite possibly it would turn over faster than this because of a supervening psychology of hope; but it would be paid out gradually over the interval, and as a whole would not gain the added velocity during the first year in order to achieve the minimum goal of income set by the President.

A PUBLIC DISCOUNT OF THE RETAIL PRICE LEVEL

The second requisite, that the new money or credit be applied as direct enhancement of mass-consumer income, would be fulfilled by paying it out as a subsidy to the retail trades.

The chief condition of such subsidy grant would be that the retail trades subtract a reversed sales tax from the price of their goods and services. It would include a discount rate given by the utilities, insofar as they dispense fuel, electric current, and other services to homes. The reversed sales tax, subtracted from the price of all goods at retail, would equal, approximately, the sum of the subsidy granted, and the retailer, thus reimbursed, would benefit only by his increased volume of sales at the compensated price.

It would amount to a public discount on the retail price level within the estimated capacity for increased income (an increase, that is, of $22,000,000,000 of income during 1938). Such increased income would be realized on the old retail price level as compensated by the subsidy.

It would retain the old retail price level; it would also retain the old wholesale price level, thus allowing contracts for future delivery to be properly based with respect to prices on the existing level of costs, but it would result in a discount on the price level at retail to consumers, allowing them to get the goods really at a lower price level, but without deflation to business.

ADVANTAGES

The change would be accomplished without disturbance to the prevailing cost-and-price system, so far as industry and the retail trades are concerned.

Yet, by the terms of issuance and payment, the subsidy would act directly to raise the real income of the people to $90,000,000,000, with restoration of employment and increased production of existing equipment, together with lowered unit costs and reduction of overhead charges incidental to such increased output.

The repercussion upon profits (which should, by all means, be held to an agreed top rate in given classes of cases upon turn-over of sales) as well as upon the stock market, would be immediate and wholesome.

The Nation's underlying values would rise soundly, as based on fuller production of existing equipment, with pronounced rise in domestic distribution. For mass purchasing power would be equated to mass productive power, at present capacity for wanted goods and services.

TRANSITION

The transition to the new financial and industrial economy would be accomplished by the cooperative organization of industrialists and Government, aided by the Congress, a cooperative organization that is now forming.

RIGHT TIME FOR A LOWERED PRICE LEVEL

When production and distribution shall have been revived to approximate the capacity of the industries with the accompanying incidental economies, a movement to reduce the price levels of basic materials and of consumers' goods would not be disturbing to business, as it would now be disturbing.

That, I think, is the crux of the problem that the President faces today. He is asking business to reduce its prices at a time when it is not in full production or anywhere near full production, when it cannot sell its goods now on the existing price level, and he is asking them to accept losses out of their own pockets on the existing economy, which is an economy with a tremendously heavy overhead and a very small current production. If a cushion could be provided, a financial cushion, by which industry could move over into capacity production without loss, and consumers' goods be swelled accordingly, then would be the time to have it if you want a general reduction in prices, because the economies that warrant a general reduction of the price level would then have been achieved.

The economies would be realized and manifest. The reduction in overhead would proportionately affect unit costs to reduce them. The Budget would be balanced. As industry advanced to new and permanent increases in productive capacity, new debt-free money might be issued by the Government to reduce the national debt and to meet current expenses, with remission of taxes, and without danger of inflating the general price level.

Now, I have here notes from the Federal Reserve Bulletin of December 1937, and for February, this month, which show that the net decline last year in total deposits at all banks, excluding the large decrease in interbank deposits, amounted to over $600,000,000. This is small as compared with the total volume of deposits, which, at about $51,000,000,000, excluding interbank deposits and items in process of collection, is as large as in 1929, when the volume of business transacted was much greater. Existing deposits, therefore, if put to more active use, are sufficient to finance a substantial expansion of business activity.

But the turn-over of existing deposits subject to demand has decreased for the reasons which I gave to your committee at the last hearing. Those who sold stocks all through last year, expecting the stock market to go down still more, kept billions of deposits inactive. They did not put them out in investments or buy stocks with them. They still expect the stock market to go down. The raising of the reserve limit resulted in the drawing down of correspondents' deposits with the New York banks, and the New York banks sold their Government securities, a billion and a half of them. The 100 largest banks of this country found that their deposits were reduced by two billions. These together with the cessation of Government spending by three billions, have resulted in the stagnation of demand bank deposits, and that stagnation is due to the debt policy, directly to the Government's having issued new money into circulation as debt.

Now, I do not believe that any of the members of this committee will question me on how money is actually manufactured. The banks manufacture it, and they issue it to the Government as debt. There is no reason why the Government should not issue that money exactly as the banks do.

Mr. **Goldsborough**. Mr. Brougham, you see it continually stated in the press, and it has been stated several times before this committee during these hearings, that the banks are full of money; and, that being so, what is the necessity of having any other or different kind of money or any new process for getting money into circulation?

My understanding is that this is not correct. The banks have the right, by exercising their fractional reserve policy, to create bookkeeping credits; but as far as money is concerned, they have practically none.

I am going to illustrate. During the worst of the depression, I will say around March 4, 1933, the banks as a whole were insolvent. Their securities were not sufficiently valuable on the markets to make them solvent, but in spite of the fact that the banks were insolvent they had some cash, and under our system that cash constituted a reserve. The consequence was that even though they were insolvent, they could still run; that is, they could still create demand deposits.

The Government did several things, one of which was this: They said—

> Yes, you are busted, and we are going to put not the actual cash valuation of your securities as their value, but what can be called a fair market value. Expressed in another way, we are going to say artificially that your securities are worth so much, so as to make you solvent when you are actually insolvent.
>
> That is one thing we will do.
>
> Another thing we will do is this: You are busted. You have nothing, so what we are going to do is to create a Reconstruction Finance Corporation—that is what we will name it—and then, although you are insolvent, we, the Government, are going to borrow money from you, and that money we are going to hand over to the Reconstruction Finance Corporation, and then, although you are insolvent and have loaned us money which we handed over to the Reconstruction Finance Corporation, we will in turn say that you are insolvent and order the Reconstruction Finance Corporation to lend you enough money to make you solvent.

Isn't that what happened?

Mr. **Brougham.** That is what happened, and that is a contradiction in terms, and it is a perfect absurdity, and it shows the illogicality of our present existing debt-creating system. Whatever money is issued or manufactured must acquire its value from the goods of the people of the United States, and from their property. It cannot acquire its value from private groups who issue it, except as they belong to the whole people. Why they should ever have had that right, or acquired that right, is past understanding, if it were not for the fact that we had to have some kind of money system, and at the time this system grew up, they did not understand what money was.

Mr. **Williams.** Is there any other system in the world?

Mr. **Brougham.** There is no other system in the world.

Mr. **Williams.** Then we are not alone on that proposition?

Mr. **Brougham.** No, sir; we are not alone on that proposition, nor are we alone in these recurring sharper and sharper depressions.

Mr. **Williams.** Has anybody in the world ever seen fit to do what you are advocating and remain solvent?

Mr. **Brougham.** They have not seen fit to do it, and they have not remained solvent.

Mr. **Goldsborough.** Let us see about that. From the time Napoleon got control of the French people until he was banished to Elba, do you know whether or not it is a fact that he absolutely refused to borrow money from the Rothschilds and from the international bankers?

Mr. **Brougham.** Of course, that is when national debts began.

Mr. **Goldsborough.** Is it not a fact that it was because Napoleon refused to borrow from the bankers, and insisted on France issuing her own money, that the bankers financed the opposition to Napoleon and finally destroyed him? Isn't that an historical fact?

Mr. **Brougham.** That is true.

Mr. **Goldsborough.** From 1921 to, I think, 1929, the same condition existed with the dictator in Spain. I do not recall at the moment his name. He refused to use the international bankers. Spain had a period of prosperity such as it had never had before, but the international bankers financed the revolution to put him out of business.

Mr. **Brougham.** If the governments will issue their own money—as the banks issue the money for the governments now—with the greater warrant for issuing it that it can be based upon the whole national credit—whereas, as the bankers issue it, it is issued on the national credit, but with an obligation of the bankers beyond what they put into it and as a debt, and with the liability that it will be recalled, and with the fears that that engenders—if the Government will issue the money debt free, and issue it to the people of the United States who own that money, because they own the values that that money stands for, it can go into trade in the normal way, it can eventuate as cash on deposit, instead of loans on deposit, and the Nation normally can go ahead as it should, and as business should, perfectly solvent, and with cash in the bank as Henry Ford has cash in the bank.

The loans will be the exceptions.

Mr. **Ford.** What kind of cash has Henry Ford in the bank?

Mr. **Brougham.** He has what they call cash credits. He borrowed a few thousand to begin with and since then he has not borrowed.

Mr. **Williams.** Your idea would be to have a society where nobody owned anything?

Mr. **Brougham.** No, sir; that would be the acme of perfection.

Mr. **Williams.** I do not see just where your theory would lead to, except to get everybody out of debt.

Mr. **Brougham.** Normally. Now, we have been brought up, you and I, with the notion that business has to be run on debt, and we confuse the word "credit" with debt, which is the opposite of credit. Credit means cash in the bank. It means credit that you can spend any time.

Mr. **Williams.** In other words, if you had the money in the bank you would not owe the bank anything?

Mr. **Brougham.** That is what business should have normally, if it were not for the fact that every dollar issued in this country has been issued as a debt to private groups, so that it must be paid back.

Mr. **Williams.** How will we get out of debt now as individuals?

Mr. **Brougham.** The individual problem is very different from the national problem, but it impinges upon the individual problem.

Mr. **Williams.** Suppose that I owe $1,000, how will I pay it off, or $10,000?

Mr. **Brougham.** Do you mean under this system?

Mr. **Goldsborough.** He means under a different system.

Mr. **Brougham.** Then——

Mr. **Williams.** Your idea, as I understand it, is to get everybody out of debt completely.

Mr. **Brougham.** Yes.

Mr. **Williams.** How are you going to do that?

Mr. **Brougham.** Let us think of the first step——

Mr. **Williams.** What is that debt?

Mr. **Brougham.** The national debt or the individual debt?

Mr. **Williams.** The composite, the complete debt obligation of this country.

Mr. **Brougham**. It has been pretty nearly, I imagine, what the estimate of the national wealth is.

Mr. **Williams**. What is it, for the individual, the municipality, the city, county, and State?

Mr. **Brougham**. At one time during the depression our national debt, according to some estimates, exceeded the national wealth.

Mr. **Williams**. What would that be, about?

Mr. **Brougham**. It is very fluctuating.

Mr. **Williams**. But what is it?

Mr. **Brougham**. Say about 200 billion dollars.

Mr. **Williams**. That everybody owes everybody else, altogether?

Mr. **Brougham**. That everybody owes everybody else, and that they owe to the banks.

Mr. **Williams**. How will you get out of it?

Mr. **Brougham**. Now, as the first step for the individual getting out of debt his purchasing power could be raised immediately by 20 percent under this bill.

Mr. **Williams**. What would you do with it if his purchasing power was raised?

Mr. **Brougham**. He would go to the store and buy goods.

Mr. **Williams**. He would buy more consumptive goods?

Mr. **Brougham**. For 15 percent less than the retailer feels he has to price them.

Mr. **Williams**. Then it would increase the consumption of goods.

Mr. **Brougham**. It would increase the consumption of goods.

Mr. **Williams**. That is the purpose of this bill?

Mr. **Brougham**. Yes, sir; and that would make a draft upon the capacity of industry.

Mr. **Williams**. That would increase his capacity to buy consumptive goods?

Mr. **Brougham**. Yes, sir.

Mr. **Williams**. And thereby increase production?

Mr. **Brougham**. Yes.

Mr. **Williams**. If that is true, suppose that he owes $1,000, and expends it all for consumptive goods, how will he pay back his obligation?

Mr. **Brougham**. If he owes $1,000 and spends it all for consumptive goods, your question is self-limiting there; he cannot pay it back; but if he owes $1,000 and he has to spend only $800 for consumptive goods, he has $200 with which to pay his debts, and, as I understand it, the purport of this bill is to enable him to do just that.

Mr. **Williams**. Then you would not expect him to spend all of it?

Mr. **Brougham**. He would take advantage of the discount and save that to pay his debts with.

Mr. **Williams**. What proportion of the people of this country are saving anything, or any material amount, now?

Mr. **Brougham**. I read to you just now a statement of the amount that the people of the country as a whole have in the banks, or what they had in 1934, about three billions.

Mr. **Williams**. Involving what percentage of the people?

Mr. **Brougham**. About 98 percent of depositors that they had in the banks in 1934.

Mr. **Williams**. But what percentage of the people of the country are making any savings at all? Not what they have in the bank, but what percentage of the people have an income over and above the amount necessary to secure the bare necessities of life?

Mr. **Brougham**. Most of them have nothing above the bare necessities of life. What they get is insufficient to meet those necessities.

Mr. **Williams**. And to put your principle into effect would simply increase their purchasing power?

Mr. **Brougham**. It does a lot besides that. It would introduce economies in production.

Mr. **Williams**. All right——

Mr. **Brougham**. And eventually will lower the prices.

Mr. **Williams**. It ought to do that.

Mr. **Brougham**. Yes.

Mr. **Williams**. And permit them to purchase more of needed goods and services?

Mr. **Brougham**. Yes; and reemploy them, and allow them to get an income, a money income, which, with the price level that is adjusted to that income and is reduced constantly, will enable them to more than meet the necessities.

Mr. **Williams**. And then pay off their debts?

Mr. **Brougham**. And then pay off their debts.

Mr. **Williams**. And we will reach the point where nobody will owe anybody anything?

Mr. **Brougham**. That, of course, will be the goal of our economy, I hope. However, the actual goal of our economy at present is to get people more and more in debt, and most of you gentlemen have been confronted with bills to get people more and more in debt. This is a bill which has a directly contrary tendency.

Mr. **Williams**. Of course, you would not have any use, under your theory and system, as I understand it, for a bank at all?

Mr. **Brougham**. Oh, yes.

Mr. **Williams**. As we understand it now?

Mr. **Brougham**. Yes; as we understand it. The historical use of a bank is to keep accounts, not to manufacture money.

Mr. **Williams**. Oh, yes; just make a warehouse out of it?

Mr. **Brougham**. To keep accounts and to handle checking accounts.

Mr. **Williams**. Just lock it all up in one vault and pay a certain percentage of it to the man for keeping it for you?

Mr. **Brougham**. Yes. He has money in the bank; he really has money in the bank, and should have.

Mr. **Williams**. But, of course, that would absolutely destroy the banking functions that we have now.

Mr. **Brougham**. There is no reason why the banks should not go on lending, or why they should not handle my account and see that my checks are properly taken care of in distant cities.

Mr. **Williams**. Whose money would you lend?

Mr. **Brougham**. My money, the depositors' money, which they would hold in trust.

Mr. **Williams**. But suppose you went in and wanted it.

Mr. **Brougham**. If you wanted it, then he would hold it on demand. As it is now, the bank owns your account. You do not own it. You only own an obligation of the bank, but under this system——

Mr. **Williams**. You can go in and get your account if the bank is solvent.

Mr. Brougham. If it is, yes. In March 1933 we did not know that it was solvent.

Mr. Williams. Of course, it would not be solvent, and no other business would be solvent if everybody should want all of their money at one time. We do not conduct business on that basis, anyway.

Mr. Brougham. I know that we do not, and that is the vice of this system.

Mr. Williams. Do you think that we ought to have a banking system so that they could pay everybody all of their money at one time?

Mr. Brougham. All of their money that is held on demand, but——

Mr. Williams. Suppose everybody should want their money all at once?

Mr. Brougham. We know they do not. We know that everybody wants normally to invest their money and hold a certain amount on demand, but, as to what is held on demand, they should have the last penny if they want it.

Mr. Williams. Then you would not have any money to lend to anybody.

Mr. Brougham. Oh, yes, because most people definitely keep a certain amount on demand, and should have that all, 100 percent, when they wanted it, and they keep a certain amount for investment.

Mr. Williams. What is the relation in this country now between demand deposits and time deposits of banks?

Mr. Brougham. You are supposed to give notice if you withdraw a time deposit. There are today about 32 billions of demand and cash deposits, and about 19 or 20 billions of time deposits.

Mr. Williams. You mean that that is all you would have to lend?

Mr. Brougham. That is all that we have today.

Mr. Williams. Under your plan, that is all that you would have to lend? You would have 19 billions to lend, you say?

Mr. Brougham. Yes. Under this system that I envisage, we would have made more and loaned more on deposit.

Mr. Goldsborough. As far as the bill that you are now considering is concerned, that would not be the situation, would it?

Mr. Brougham. We would have more on demand and more on deposit, on time deposit.

Mr. Goldsborough. There is nothing in this bill which, even if the bank is not on a 100-percent basis, would change the ownership of those deposits.

Mr. Brougham. No. This bill still continues the fractional deposit system.

Mr. Williams. Your plan provides for 100-percent reserves.

Mr. Brougham. No; it does not.

Mr. Williams. I am talking about this particular bill. You have been talking about generalities here.

Mr. Brougham. I hope not.

Mr. Williams. Does not the general scheme that we are considering here, and that you are talking about, provide for 100-percent reserves in the banks?

Mr. Brougham. It provides for a condition by which we could easily achieve 100-percent reserves on demand deposits, and I think that it is possible at this moment, during this Congress, to have 100-percent reserves without hardship to the banking system.

Mr. Williams. Do you believe in that?

Mr. Brougham. I certainly do, implicitly.

Mr. Williams. You believe in 100-percent reserves in the banks?

Mr. Brougham. Yes, sir. All that Congress would need to do would be to allow the banks to get the reserves.

Mr. Williams. I do not understand how you have any money to lend if you have to keep it all locked up 100 percent.

Mr. Brougham. I did not say that. You said that.

Mr. Williams. I say, I do not understand that.

Mr. Brougham. I do not, either.

Mr. Williams. That is Mr. Goldsborough's position, I understand.

Mr. Goldsborough. No; that is not my position. There is nothing in this bill which would change the ability of the banks to loan. They would loan exactly as they loan now, and the mere fact that more money went into circulation, which would get into the banks and which would increase their reserves, would not diminish in the slightest sense their ability to loan just as they loan now, and just as much as they loan now. The difference would be that because of this continuous cushion under the retail sales, that the banks would always be guaranteed such a market as would make it impossible for their securities ever to go to pieces.

Mr. Ford. Might I ask this question in that connection? Assuming that the philosophy embodied in this bill were adopted, and this went on, when the bank does loan any money, would that loaned money create new money?

Mr. Goldsborough. Just as it does now; yes, sir.

Mr. Ford. It would?

Mr. Goldsborough. Yes.

Mr. Ford. What you are driving at is to get us into a debt-free condition, but you would still have debts, and those debts would create money, would they not?

Mr. Goldsborough. Let me illustrate that, Mr. Ford, in this way: Suppose that the banks, instead of having actual money in their vaults amounting to six or seven billion dollars, had actual money in their vaults equal to their present potential power to loan. The only difference would be that, instead of loaning on a fractional reserve, they would loan on a 100-percent reserve.

Mr. Ford. That would not create new money?

Mr. Goldsborough. No; and the only possible difference would be this, that if everybody did come for their money, they could get it.

Mr. Patman. With respect to that premise, instead of having 6 or 7 billion dollars in cash, as they have now, is it not a fact that they have only about 800 million dollars?

Mr. Goldsborough. But they do have capital, surplus, and undivided profits.

Mr. Patman. That is true, but that is not necessarily money.

Mr. Goldsborough. That can be converted into cash of about 7 billion dollars.

Mr. Spence. Do you believe in the 100-percent reserve idea?

Mr. Brougham. I do; but I agreed at the last hearing not to talk about that, because it mixes this bill up.

Mr. Spence. Does not the banker have to give you back, then, the same money that you put there?

Mr. Goldsborough. I think there is a misunderstanding, Mr. Brougham, between you and Mr. Spence and Mr. Williams. I am discussing this particular bill myself. I do not know whether you are discussing something else.

Mr. **Brougham**. I would like to discuss this bill.

Mr. **Goldsborough**. Under this bill, even though the banks were required to carry 100-percent reserves, they would still be the owners of the deposits—that is, under my bill. They would not be warehousemen at all, would they?

Mr. **Brougham**. No.

Mr. **Goldsborough**. And they could loan the deposits exactly as now?

Mr. **Brougham**. It is the same system that they have now.

Mr. **Reilly**. But they would have to keep a 100-percent reserve.

Mr. **Goldsborough**. Why?

Mr. **Reilly**. If I put up $10,000 in the bank on a checking account they cannot loan on that, because just as soon as they do they do not have a 100-percent reserve.

Mr. **Goldsborough**. Of course they have. They still have the cash. The only thing that they loaned you is the credit.

Mr. **Reilly**. They have the cash, subject to the depositor's check, and they could not loan a dollar of that 100-percent reserve.

Mr. **Goldsborough**. You are as mistaken as you could possibly be. There is not a particle of difference.

Mr. **Reilly**. If I put $10,000 in the bank and they loan some of that to John Jones, my 100-percent reserve is not there.

Mr. **Goldsborough**. You are mistaken, because they do not take the cash out of the bank's vault. They simply loan the bank's credit, just like they do now.

Mr. **Reilly**. What do they loan it on? If they make the loans on their deposits then they do not have a 100-percent reserve.

Mr. **Goldsborough**. Of course they have, unless they loan it in cash.

Mr. **Reilly**. I have gone to the bank and taken out cash on my notes. Lots of people do that. This idea of loaning credit is only a partial picture of the banking situation, because any number of people go to the bank, put their notes in, and take the cash out. It is done every day.

Mr. **Spence**. I believe that Professor Fisher has the same idea that you have about the 100-percent reserve, and I think it is that the banks cannot lend that money, and that the way a bank will obtain money is through a service charge.

Mr. **Goldsborough**. Under his plan, but there is nothing like that in this bill.

Mr. **Williams**. I do not see myself how this bill would operate.

Mr. **Ford**. Here is a bank that has $500,000,000 of demand deposits. Against that $500,000,000 the group that owns that bank must have in their vaults an additional $500,000,000 in order that they shall be solvent and that there shall be no fractional reserve.

Mr. **Crawford**. Will the gentleman yield there?

Mr. **Ford**. Yes.

Mr. **Crawford**. When these deposits are put in, will you state for my information whether or not they go in in the form of currency or of bookkeeping entries, in your illustration?

Mr. **Ford**. Both forms.

Mr. **Crawford**. If you put them in in both forms, you confuse the issue.

Mr. Ford. No, you do not; because everybody does not deposit by check. A lot of them deposit cash.

Mr. Crawford. But if they come around and ask for currency, where will you get the currency unless it is put in? I understand how the thing operates at the present time, but I am trying to get back to Mr. Goldsborough's illustration, where he tried to bring in the idea of bookkeeeping.

Mr. Goldsborough. I think that I can clear that in 2 or 3 minutes, if you gentlemen will let me.

Let us assume that the bank has in its reserves a million dollars in cash. Then it can loan $1,000,000 as far as bookkeeping is concerned.

Mr. Williams. You cannot do it if you are required to keep it as a reserve.

Mr. Transue. Let me ask you this——

Mr. Goldsborough. Banks can lend now on bookkeeping credit tantamount to the cash that they have, but if anybody comes after the cash, even though the bank's capital, surplus, and undivided profits have not changed, then that decreases their reserves just exactly as it would be on the 100-percent basis.

Mr. Transue. Suppose that a man goes in and borrows $1,000 and they write a check for $1,000. When that check comes back to the bank don't they have to give up another $1,000?

Mr. Goldsborough. Not under our system, not in cash; no.

Mr. Transue. Well, suppose this transaction, that I want to borrow $1,000 and they write a check, and I give that check to Mr. McKeough, and he takes it to the bank and says, "I want $1,000." That would be the equivalent of a cash transaction, would it not?

Mr. Goldsborough. I will illustrate the way that we do it now. Let us assume that now, under the present process, a bank has $100,000 in cash. That gives the bank in its reserves the right to loan $1,000,000.

Now, suppose that somebody were to come in and say, "You owe me, and I have on deposit, $50,000, and I want it in cash," and the bank hands the depositor $50,000. Then the bank would have only $50,000 in its reserve against the $1,000,000 which it has loaned out. Then the bank examiner would come and examine the bank and say, "You have to call in $500,000 of your loans, because your reserves have gone down to $50,000, and you have got loaned against those reserves $1,000,000, and you have simply got to call in half a million dollars of what you have loaned."

Now, exactly the same condition would exist under the 100-percent system. As long as you had the money in the bank, you could loan against it dollar for dollar, and if anybody took the money out of the bank, you would have to call in your loans.

Mr. Transue. What you are getting at is, you would loan 10 times what you have now, and with the 100-percent system you would loan just one time?

Mr. Goldsborough. Just an equivalent amount, and keep out an equivalent amount, and that is all you could ever do, and the banks would be no worse off than they are.

Mr. Transue. Under that system the banks would loan one-tenth of the amount they can loan under the present reserve system.

Mr. Goldsborough. Yes; but they would have 10 times as much to loan, because they would have the actual money on deposit.

Mr. **Patman**. Will you let me ask a question there? Are you through?

Mr. **Transue**. I will yield.

Mr. **Goldsborough**. When you get it into your minds, it is just as simple as it can be.

Mr. **Patman**. I am really trying to see it.

Let us assume that you have a bank with a capital stock of $1,000,000. You have just organized it, and you have extended loans amounting to $1,000,000, and Mr. Ford comes in——

Mr. **Goldsborough**. Is that under the present system?

Mr. **Patman**. Yes; and under your system.

Mr. **Goldsborough**. Under a 100-percent system?

Mr. **Patman**. Mr. Ford comes in and deposits $1,000,000. You have got an actual 100-percent reserve, and I go over and borrow that $1,000,000.

Mr. **Goldsborough**. What do you do with it? Do you take it in cash?

Mr. **Patman**. Yes.

Mr. **Goldsborough**. Then the bank has not anything more.

Mr. **Patman**. If you owed him a million and you owed me a million and you only had a million, that is a 50-percent reserve, and, in fact, you have not got anything.

Mr. **Goldsborough**. You cannot loan except an amount equivalent to whatever cash you have.

There is not a thing complicated about this.

Mr. **Reilly**. You talked about banks loaning 10 times their deposits.

Mr. **Goldsborough**. No; I did not. That is a very different thing. Ten times the cash they have.

Mr. **Reilly**. As a general proposition, the statement is made that when a bank takes $10 of my deposit, it can loan 10 times that much.

Mr. **Brougham**. That is incorrect. They cannot.

Mr. **Goldsborough**. They cannot do it.

Mr. **Reilly**. That is the common statement that you hear over the radio and everywhere else about the bankers making extensive loans on deposits.

Now, I want to read what the Comptroller of the Currency says about banks today. On the date of this last report, there were 15,580 National, State, and private banks. Their total loans and investments were $49,972,000,000. Their total deposits were $59,822,000,000.

Mr. **McKeough**. What are the total loans in that statement?

Mr. **Reilly**. Let me finish. Under this 100-percent deposit, the only money the banks could lend would be its capital stock.

Mr. **McKeough**. Does it show the total loans as of that date? You merely mentioned the investments of the bank.

Mr. **Reilly**. That means loans and investments of the banks, $50,000,000,000.

Mr. **Goldsborough**. I will make one suggestion, if you will let me do it, and that is that there is a complete misunderstanding almost everywhere on just what banks can loan against. The banks do not loan against their deposits. They do not loan against their capital stock, their surplus, or undivided profits. They loan against the actual cash which they have, and that involves their loaning capacity. If they have $20,000 in cash, either in their own bank or reserve, they can loan $200,000, but it is against the cash.

Now, think about it between now and tomorrow, and you will find that there is really no difficulty, in my opinion, about this 100-percent reserve.

Mr. Crawford. You say cash. Do you mean cash or its equivalent?

Mr. Goldsborough. Of course. Cash or a reserve that they can draw on.

Mr. Crawford. I say that to clear the record, because somebody will read this and say that you were wrong.

Mr. Williams. Who fixes the 10 percent?

Mr. Goldsborough. How is that?

Mr. Williams. Why do you say 10 percent, or 10 times?

Mr. Goldsborough. Well, of course, under the ruling of the Federal Reserve Board, it is now less than 10 percent, Mr. Williams, but I was figuring it under our ordinary system.

Mr. Williams. Where is there any rule or any law that fixes it?

Mr. Goldsborough. The law was a matter of custom under the Federal Reserve Act as amended during the war, but it now specifically provides in the Federal Reserve Act that the reserves shall be 7, 10, and 13 percent. Most of the reserves required are 10 percent.

Mr. Williams. That is in reserves; yes.

Mr. Goldsborough. But that means cash.

Mr. Ford. Might I make an observation there?

Mr. Williams. It has been raised to 14, 20, and 26.

Mr. Goldsborough. That is correct.

Mr. Ford. We have in this country many insurance companies that issue policies to pay on a man's demise, and there is always a great volume of that "Johnnie-on-the-spot" money paid when a man dies, but is there an insurance company in the United States that could pay its death benefits if everybody having those policies suddenly died?

Mr. Transue. There would not be any need to pay them then.

Mr. Ford. No; there are a lot of people who are not insured.

Mr. Goldsborough. The insurance companies were confronted with a terrible situation in 1918.

Mr. Ford. I know.

Mr. Goldsborough. And what they do they can do with mathematical accuracy; they can figure on what deaths will take place and act accordingly; but if everybody were to die, they would bust.

Mr. Ford. That is an actuarial proposition.

Mr. Goldsborough. Yes.

Mr. Ford. And I asked the other day if there are any actuarial figures on banking that take into consideration what the bank might suddenly be called upon to do. Has that ever been worked out?

Mr. Goldsborough. No, sir; and if you want me to give you the history of that, I can do it, but we have not the time to do it now. That grew up in England among the goldsmiths, and they finally reached the conclusion that only about 10 percent of the gold would be called for, and they decided that they could loan out on that basis.

Mr. Ford. I read some place not long ago that the Canadian banking system employed an actuarial system on the handling of their loans and discounts and their deposits and investments.

Mr. Brougham. May I submit, as a part of my statement, a memorandum on the Proposed Capacity System, Inc.?

The Chairman. Without objection, that may be done.

(The memorandum referred to is as follows:)

Memorandum on Proposed Capacity System, Inc.

(By Herbert Bruce Brougham, Mount Vernon, N. Y.)

It is common knowledge that industry in the United States is running, on the average, less than 6 hours daily. But only lack of orders prevents the running of American industry on an average of 12 hours or 18 hours daily, with suitable work shifts.

The published conclusions of the Brookings Institution, of Washington, have stressed the necessity of a general lowering of prices by trade and industry in order that the entire product of its facilities running at capacity may be brought within the purchasing power of the people.

At first sight such proposal appears to be impossible. All business entails contracts for future delivery; contracts made upon a given level of costs cannot be properly discharged upon a lower level of prices.

In fact, Dr. Moulton, president of the Brookings Institution, in his article (Fortune Magazine, November 1935), which summarizes the Brookings researches, seems to overlook the dual nature of the problem. There is (1) the problem of cutting prices to the point where the people can buy the products of industry at full capacity for wanted goods and services. But there is also (2) the problem of maintaining the general price level stable for all contracts for future delivery.

The proposed Capacity System, Inc., would provide a financial cushion by means of a circulating trade-discount system, as a practical method of lowering the price level to the consumers at retail. At the same time it would preserve the wholesale-price level to producers and the retail-price level to distributors by reimbursing them for their discount allowances by an equal amount of circulating trade credits on the books of jobbers and wholesalers; by the jobbers and wholesalers ,in turn, the trade credits would be passed back to manufacturers and prime producers; and by all classes of producers and distributors the trade credits would be paid to labor and circulated among the various classes of producers and distributors as an addition to their working capital.

Issued to motivate the margin of unused capacity for output of wanted goods and services, and kept within such margin, the trade-credit issues would stabilize the wholesale-price level on an expanding program of production and distribution.

This can be done without reform of the present money-and-banking system. It can be accomplished without political agitation or the passage of new monetary measures. It is practicable in the entire field of extractive industries and in manufactures and trade that are advantaged by the mechanical improvements of the present age.

Moreover, it accords with recent industrial precedent.

Thus individual manufacturers have proved it possible to cut the price of their products to a point even below cost in order to evoke an influx of new orders in permanently added volume and to step up their factory operations in order to achieve the economies of capacity production, with low overhead, and profits assured at the lowered prices.

NO INSURANCE HITHERTO AGAINST RISKS

The industrialist who accomplished this feat acted singly and at a great risk.

Not all of them succeeded, as Henry Ford succeeded. The majority, quite possibly, have been like Durant, of Durant Motors, unsuccessful. The pioneer industrialist, indeed, devised no financial cushion for their initial operations of price cutting and many ran into great losses. They evolved no mutual insurance system to provide for the transition to a lower price level, the financial equivalent of the economies to be achieved, and to balance such economies by means of trade credits wherewith to reimburse all the factors concerned in apportioning the price discounts to their customers.

Moreover, these first price cutters did not know how to meet the risks involved in a defective money-and-banking system.

They might have done so had they paused to reflect that banking is essentially bookkeeping, properly a function of business.

A circulating trade-credit system becomes necessary, chiefly because banking has grown up divorced from the productive system to which it has no integral relation. Bank issues of monetary credits have never been adjusted, in the main, to the realizable volume of production with existing industrial equipment; rather they have been used to manipulate price levels and inflate or depress them for speculative purposes.

BROAD BASIS OF INSURANCE IS PRACTICABLE

To remedy this defect of bank bookkeeping the proposed Capacity System, Inc., would amalgamate the manufacturing and trading interests of localities; first, in the metropolitan areas of the United States, finally to extend over the entire country, by a system of circulating trade credits based on unused but available capacity for wanted goods and services, which would permit of direct discounts on retail price to consumers.

A CONTINUOUS SURVEY OF CAPACITY

A board of survey and estimate, aided by management engineering counsel, can be provided to maintain a continuous survey of capacity and to weld the body of producer-and-trader members into an organic body functioning at capacity.

Applications for membership from retailers, jobbers, manufacturers, and prime producers can be favorably received as fast as the volume of retail customer orders increases by the inducement of a generous price discount. Each member, as admitted, may be assured that the management will calculate upon, approximately, capacity output of existing equipment and labor, with the economies this entails, for him and for all participating members.

WOULD SUPPLEMENT BANK CREDITS

It should be recognized that bank credits now supply the financial means to keep business going only at a fraction of its present capacity.

The proposed trade-credit system is designed to supply a supplementary means to keep business going for its present unused margin of capacity.

It is expected, therefore, that the volume of circulating trade credits, monetizing such margin of unused capacity, would be increased progressively in order to make eligible for membership every concern that can supply the community with wanted goods and services.

The volume of trade credits can be augmented in the ratio of net turnover of production as consumer income, and within the capacity of existing equipment; in the ration; that is, of $1 of trade credit to $3 of expected realizable income per year. Such turn-over three times yearly would tally with the usual turnover, in so-called good times, of cash and demand bank deposits as consumer income.

The greater the margin of present unused capacity, while applications for membership flow in, the larger the volume of the permissible trade credits and the larger the possible discount to customers at retail, until the facilities of incoming members shall approximate the "saturation point" of real demand of the community for goods and services.

PROPOSED RETAIL-PRICE DISCOUNT

Let us assume that the discount fixed for the first month's operation of Capacity System, Inc., is 25 percent; and that this discount of 25 percent shall be in force until the entire appropriation of trade credits, issued in the ratio of $1 in trade credit to $3 worth of goods and services issued on the realizable margin of yearly production at capacity, shall be exhausted.

Such retail discount would be applied to rentals of homes; as free down payment on purchases of homes, and to purchases of foodstuffs, clothing, fuel, and of all other consumables on individual and family account, and not for resale.

A discount of 25 percent would immediately increase by one-third, or 33⅓ percent, the purchasing power of all retail customers of Capacity System, Inc., and of its workers until the appropriation for the first production-and-trade cycle should be exhausted.

The annual net turn-over of such trade credits, after the first year, would then be 3 to 1. If the present margin of unused capacity is 50 (total capacity equaling 100), at the end of a year the circulating trade credits should suffice to maintain production, with its attendant economies, at approximately full capacity for wanted goods and services.

HOW TRADE CREDITS WOULD REIMBURSE MEMBERS

The trade credits would be used, initially, to reimburse the retail dealer members in the sum of the discounts allowed by them to their customers. The retailers, as they renewed their stocks of goods or bought services, would receive this sum in reimbursal to their credit on the books of jobbers and wholesalers and on the books of the system to pay, in part, their employees.

The jobbers and wholesalers in turn would receive an equal sum to their credit on the books of member manufacturers, and they as well, on the books of their supply houses and of prime producers, who would circulate the credits back to other member concerns for supplies and equipment, and in payments to their labor.

EMPLOYEES AS RECIPIENTS OF TRADE CREDITS

Inducement to acceptance by the employees of members of Capacity System, Inc., of a percentage of their wages and salaries in trade credits accruing to their employers may be realized by honoring such credits at retail as though they were cash, and as commanding in turn a like discount as cash of 25 percent upon all goods and services for individual and family consumption.

Thus the employees would find their total real wages increased by 33⅓ percent, as measured by their ability to buy with the same nominal wages 33⅓ percent more in goods and services at retail than before—including rentals of homes, down payment on purchases of homes, theater tickets, passenger transportation, hospitalization, etc.

A small increase in nominal wages, too, to all workers who accepted in trade credits a stated percentage of their pay would, of course, serve as further inducement to assure the cooperation of workers as consumers, including the multitude of workers employed by the basic industries.

CAUTION RECOMMENDED IN FIXING SIZE OF DISCOUNT

But the appropriation of trade credits must be kept within the actual proved extra capacity of existing equipment and labor to supply added goods and services on demand. It will require careful foresight to fix the size of the retail discount from month to month large enough constantly to absorb production of wanted goods and services at the rated capacity of the system to supply them, and as such capacity becomes augmented by added inventions and superior forms of organization. It will require like foresight to keep the discount rate constantly low enough, on the other hand, to prevent overdemand, with resultant undue increase in the general price level. A fairly constant price level would indicate that the prevailing discount is not set too high.

DISCOUNT RATE AS PRICE-LEVEL STABILIZER

Should the general price level rise the discount must be decreased or suspended altogether until prices return to their normal level. Should the price level fall the discount should be increased until average prices rise to the normal level.

On the cost-accounting side the device of circulating price discounts based on the percentage of unused and recoverable capacity from month to month would be the means (for which management engineers have hitherto searched in vain) of making the price system work so that the public will pay only for what it actually consumes (in material, muscles, practical skill, and machine-and-plant depreciation).

It should result in making the public replace by its payments only so much as the public withdraws by its purchases.

By circulation among the members of the new and added means of payment (trade credits), an addition to working capital would be set up on the books of the membership of Capacity System, Inc., in exactly the right quantity, and this would be put directly into the money stream to make the payment stream flow at the same rate as the price stream.

The circulating trade-credit warrants would form the equivalent of an internal money system, for the amalgamation of production and trading units, precisely to supplement and complete the external money system of cash and checks drawn against bank deposits, and in a manner to make the total means of payment (cash and checks plus trade-credit warrants) respond adjustably to the realizable increases in productive capacity of existing equipment.

THE DUAL-CREDIT SYSTEM OF SWEDEN

Sweden currently maintains a publicly licensed money system for domestic trade, which supplements its money system for foreign exchange of goods.

But Sweden's dual currency and credit system (foreign and domestic) is not yet scientifically related to any current estimates of the capacity of the productive and distributive system of Sweden.

In contrast, the dual-payments system proposed herein is scientifically related to monthly estimates of capacity for wanted goods and services.

The proposed system of circulating trade discounts tries to fulfill the double requirement of keeping stable (for purposes of the contract system) the general price level; this is done by reimbursing all producers and dealers in return for the trade discounts allowed by them, turn and turn about, out of the new volume of circulating trade credits.

Such new volume of trade credits represents the values of new economies achieved by stepping up to capacity production; meanwhile the public gets, in the discount on retail price, enhanced real income (more for its money) permitted by the same stream of adjusted trade-credit payments.

FINANCIAL CUSHION FOR LOWERED CONSUMER PRICES

Thus the combined discount and trade-credit system forms a financial cushion, anticipating and realizing, in terms of present income, the economies which it evokes, by swelling the volume of customer orders at retail up to the capacity of the system to fill such orders.

A PROBLEM OF MANAGEMENT ENGINEERING

As conceived herein, the work of organizing Capacity System, Inc., is essentially a work of management engineering.

It would require only 1 month's preliminary charting of the idle time of all prospective members of Capacity System (allowing for seasonal changes for the other 11 months of the year) in order to make the proper physical adjustment of units and have the system, as nearly as may be, a balanced organism, supplying in sufficient variety and quantity the standard brands, and grades, and styles, and services demanded by the general public as ultimate consumers.

To this end the system should supply everything represented in a standard family budget.

It should, therefore, include in its membership all the retailing, jobbing, manufacturing, transporting, and raw-materials factors for producing and distributing the required goods and services. In this process it might be guided, in part, and on the side of quality, by the tests of materials and services made by the Bureau of Standards at Washington, standardizing quality by grades and taking these into account, as well as quantity, in arriving at constantly more accurate estimates of capacity in terms of cash and trade credits.

A MANAGEMENT ENGINEERING COUNCIL

Each applicant for membership should be required to present to a management engineering council his own estimate of unused capacity of his existing equipment and labor for handling added orders for a year to come, and as reckoned on the basis of the maximum possible daily work shifts.

Such estimate should then be checked by the progress charts and idleness-expense charts of the consulting management engineers of the engineering council.

The total of such chartings would be utilized as the basis of valuation, on the average prevailing price level, or unused and realizable capacity of existing plant, equipment, and labor of all the membership.

On such valuation of realizable and recoverable capacity, the volume of new trade credits would be controlled, always, of course, with reference to the expected yearly net turn-over of payments as income of consumers.

Valuation of the net increase in capacity of the whole system would thus be ascertained each month, and such ascertainment would be used as basis for readjusting the retail discount rate for each succeeding monthly period.

TRADE WITH NONMEMBER CONCERNS

As Capacity System, Inc., would not at first comprise all of the trades, industries, and agents of transportation in its voluntary membership, there would be the problem not only of dealing with outside nonmember concerns but of reckoning how such trading will affect the estimates of unused capacity for the purpose of fixing the retail discount on price and of issuing the required trade credits for use among the membership.

For purposes of such monthly discount-rate estimates, the goods and services delivered, or "exported," by the membership to concerns outside Capacity System, Inc., would be reckoned as used capacity, or consumption; while goods and services bought of outside concerns, or "imported," into the plant and productive and distributive operations of Capacity System, Inc., would be reckoned as production.

The "export" and "import" trade with outside concerns, including, of course, foreign trade by the membership of Capacity System, Inc., would be managed with currency and demand bank deposits of the system, as is now customary.

The "exports" to outside concerns would naturally be paid for with currency and checks on demand bank deposits; such payments would suffice to finance an equal volume of "imports" from outside concerns.

DUBIOUS POLICY OF CUTTING PRICES TO OUTSIDERS

It would be a matter of policy, to be decided by the governing board of Capacity System, whether competitive exports to outside customers should be aided by subsidies, given in the form of trade credits to the exporter members, in order to enable them to undersell the general outside market.

It would be like the present policy of Japan.

Application of Japan's trade policy of giving a price discount to outside nations, financed by export subsidies of trade credits, would result in diminishing by the amount of the subsidies the possibility of consumption by domestic consumers and to reduce in proportion the discount allowable to retail customers.

Japan's policy is actuated, of course, by the wish of its industrialists to import munitions of war, machinery, and raw materials needed for Japanese manufactures. This consideration is not strong with American industrialists, who are already well equipped both with machinery and with raw materials, and whose problem is to augment, as rapidly as possible, the purchasing power of their domestic customers.

Probably the industrial and business groups formed in each metropolitan area by Capacity System, Inc., would be self-contained by more than 90 percent, especially if the system of metropolitan areas were affiliated and operated by free interchange of goods and services with each other. As these areas enlarged their membership, and as their boundaries converged and became coterminous, they would command all the trade and productive facilities of the United States, together with the economies of controlled production and delivery, at the capacity of existing facilities.

Such economies would automatically further reduce unit costs, thus enabling the membership to compete successfully with "foreign" competitors—who would not be on the capacity basis and would be subject to extra charges on account of large margins of idle overhead—and this without need of any grants of subsidies.

SUMMARY OF ADVANTAGES UNDER PROPOSED TRADE-CREDIT SYSTEM

1. The prime advantage of the system of trade credits proposed herein is that of complementing the multiple-barter system now provided, quite inadequately, by currency and demand bank deposits, and of relating it to the real demand and the real capacity to supply such demand by means of an additional circulating means of payment (trade credits) supported by margins of capacity for production of wanted goods.

2. The second advantage is this: That such complementary system of circulating trade credits would be applied initially at the point whereall industrial and trade costs must eventually be paid, namely, at retail.

The new process begins with an increased volume of induced consumer orders delivered at a discount upon the existing level of retail prices.

The volume of consumer orders, augmented by inducement of the discount, is then regularly passed back to jobbers, manufacturers, and prime producers for replacement, thus drawing on their combined output at approximate capacity for wanted goods and services. These, in turn, with the attendant economies of capacity production, are enabled to fill the volume of new "repeat" orders at an agreed rate of profit on their turn-over of sales (a rate of profit in each case made mutually satisfactory to the parties in trade).

With lowered unit costs, adjusted for the full-capacity production attained, the entire level of wholesale prices can then be properly reduced both for internal and for external trade.

3. As this stepping-up to maximum production would be done on a system of voluntary contracts, based on inducements and not on legal compulsion; and as it would not interfere with the existing banking system in any particular, no new laws would be needed to effectuate the system.

No political agitation would be required.

The precedent already set by American businessmen to cut prices, in order to enlarge a great national market, and to realize the economies of capacity production and distribution, would be followed by a new alinement of industries and commercial concerns, operating as a system of accounting related directly to their ability to fill orders.

4. By making Capacity System, Inc., their central purchasing and selling agent with outside concerns, including foreign commerce, the members would be enabled also to use the system as a clearing house for settlement of all outside currency and credit demands.

COMMENT BY EDWARD F. HARVEY

Certain additional advantages are set forth by Mr. Edward F. Harvey, engineer-banker, of Philadelphia, to whom the proposal has been submitted, as follows:

"It appears that the idea behind Capacity System, Inc., might be made highly profitable to the members, so long as the credits were kept in constant circulation and carefully steered through a complete trade cycle. There is no doubt that they have a complete self-liquidating trade cycle so long as they are kept in active circulation, and not overissued. In this respect they may be regarded as identical in principle without existing commercial-bank trade credits. But they differ advantageously in several respects from the latter.

POSSIBLE CONVERSION OF TRADE CREDITS INTO CURRENCY

"Upon occasion—which is unlikely—the proposed trade credits could be converted into currency by the establishment of an insurance fund. All producer and distributor members might set up a sinking-fund account on their own books in currency withdrawals from their banks, respectively, to offset, in the ratio of about 1 to 10, the average amount of discount vouchers that pass through their hands. This would work something like a self-insurance fund and would correspond to the fractional reserve system of the banks. Provision might be made in the charter of Capacity System, Inc., for such insurance fund, to be supported by the members out of their annual surpluses, on a pro rata or premium basis.

TRADE CREDITS, COSTLESS AND DEBT-FREE

"The discount trade credits have the advantage of originating at the point of consumption without initial obligation (that of bank-credit debt), instead of at the point of production with initial (bank-debt) obligation, which regularly attaches to every new issue of bank money. But the moment the trade credits are issued they establish their own obligation, which liquidates itself at the end of each cycle, provided the trade credits are kept in perpetual circulation.

"It is confidence that the existing commercial-bank trade credits are convertible into national currency that facilitates the acceptance of them by the public at large. When they fail to be convertible, as they do too frequently fail, a minor financial crisis is brought about. The winding up of Capacity System, Inc., might bring about a similar localized crisis; but in the latter case it would have to be admitted that a quid pro quo had been built up to offset the apparent disappearance of a section of the circulating medium.

WOULD BE SUCCESSFUL AS GOING CONCERN

"The system can work successfully if it is properly managed and kept moving, and if, as the result of the preliminary discount advanced, an equivalent expansion of production is realized that will lower net costs sufficiently to offset the reduction in price. The system differs advantageously from the commercial credits of the banking system in these particulars:

"1. They are baked dollar for dollar, in goods and services on demand, whereas commercial bank credits are backed by a fractional reserve of only about one-tenth in currency. In addition, by the self-insurance system suggested above, Capacity System, Inc., may have the benefit of a fractional reserve of currency identical with that of the banks, besides being backed 100 percent in goods and services upon demand—a 100-percent reserve which the banks never had.

"2. The credits cost the cooperative membership nothing, as they are simply the equivalent of the unused productivity, now wasted, and the economies achieved on a maximum scale of production the capacity for which is already owned by the system. The trade credits based on such economies owned by the system dispense with the obligation of obtaining commercial credits that would otherwise be needed to supplement as added debt the means of payment required for the regular conduct of business.

"3. The system initiates trade credits at the point of consumption instead of at the point of production for goods already sold in added volume, thus eliminating timing and assuring the immediate conversion of the credit into consumption, followed by equivalent replacement. For, unlike bank credits, such trade credits are backed 100 percent with goods and services ordered before the credits are applied, and well within the capacity of the system to deliver upon demand.

"4. The credits it gives rise to are perpetual, as distinct from commercial bank credits, which are constantly being recalled and reissued as the trade cycle progresses. Moreover, bank credits are often embarrassingly withheld, contrary to the general interest of business.

"5. It enables the consumer to create his own replacement demand and thus improve his occupational status and earnings.

"6. If its effect is to sell goods below cost, it does so only temporarily, in order to increase production and to make costs lower. This method has been proved successful in the existing commercial and industrial system, and should be more successful under a plan of this nature.

"7. Commercial credits in the banking system are the exact reverse, for they are built upon commodities produced, or to be produced, with a certain risk that they may not be salable and actually consumed. Commercial bank credits are perpetual only as a whole in theory; in fact, commercial credits have during considerable periods been recalled generally and not reissued, destroying accommodations to business at times when they were most vitally needed. They are also related to the national currency, which results in the need for currency reserves in the banks, so that if the holder of any definitive unit of this bank credit desires to convert it into national currency, he may do so, within limits. Such limits become painfully restricted when the fractional reserve system of the banks breaks down, as was the case early in 1933."

Mr. GOLDSBOROUGH. The committee will meet tomorrow morning at 10:30, when we will resume the consideration of this bill.

(Thereupon, at 12:20 p. m., an adjournment was taken until Wednesday morning, February 16, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

WEDNESDAY, FEBRUARY 16, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on H. R. 7188 were resumed at 10:40 a. m., Hon. T. Alan Goldsborough presiding.

Other members of the committee present: Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Transue, Mr. Barry, Mr. Luce, and Mr. Crawford.

Mr. Goldsborough. The committee will come to order.

STATEMENT OF HERBERT BRUCE BROUGHAM—Resumed

Mr. Goldsborough. Mr. Brougham, in the discussion yesterday morning, I think you and Mr. Reilly, and possibly Mr. Williams—I do not remember about Mr. Williams—in discussing the 100-percent reserve, had in mind, all three of you, the plan that is set forth in Professor Fisher's book.

Mr. Brougham. Yes, sir.

Mr. Goldsborough. I want to ask you a question, but I want to clarify it before I do.

I have had a great many discussions with Professor Fisher about a possible 100-percent plan, and his views and mine are just as divergent as they can be. I have never seen any necessity at all for changing the present operations of the banks, and any change in their operation is not involved in this bill at all, as I think you will see, if you will read it carefully——

Mr. Brougham. I agree with you.

Mr. Goldsborough. Now, Mr. Brougham, the reserve requirements have already been raised 100 percent, as you know.

Mr. Brougham. Yes, sir.

Mr. Goldsborough. There has been no change in the operation of the banks?

Mr. Brougham. Not at all.

Mr. Goldsborough. They operate just like they did before.

Now, then, suppose that in the course of time, by virtue of the use of this discount involved in the bill now under discussion, as the discount money supplanted the reserve money, and the reserves therefore were raised so as to prevent an inflationary condition, we reached a point where the banks would be on a 100-percent reserve. When that time arrives, I want to illustrate what I conceive to be the difference in the situation now from what it will be then, and see if you agree with me, and we will take as an illustration a bank which now has in cash, in its reserves $100,000.

Under the law as it was before the reserve requirement was raised, the bank could loan a million dollars, when it would have a million dollars on deposit.

Now, then, if through the operation of the discount provided for by this bill some bank finally acquired, instead of $100,000 in its reserves, $1,000,000, and the reserves had been raised to 100 percent, it would have $1,000,000 in its reserves but it would still only have $1,000,000 to loan and only a million dollars on deposit.

Mr. Brougham. That is very possible.

Mr. Goldsborough. So that, insofar as the operation of the bank is concerned, it would be exactly as it is now. It would have as much money to loan as it has now. The only difference would be that it would have real money to loan instead of a fractional reserve privilege.

Mr. Brougham. That is true.

Mr. Goldsborough. That would be the only difference, and this money would be in its reserve, and it could control any check money and bookkeeping money exactly as it does now. That is correct, is it not?

Mr. Brougham. Yes. I believe I was wrong in stating, I think, in response to a question by Mr. Williams——

Mr. Goldsborough. Wait just a minute. I will clarify that for you.

Mr. Ford. You said something yesterday, while I think about it——

Mr. Williams. I want to ask you something about it today.

Mr. Brougham. I think I was wrong in assuming that under the set-up of your bill there would be a change in the legal status of those deposits under the 100-percent reserve as arrived at through your bill. There would be no change from now. Under the law now, the bank owns the deposits of its customers——

Mr. Goldsborough. Yes.

Mr. Brougham. And has traded for those deposits its obligation to pay upon demand, but that would remain the same. Under Professor Fisher's plan, the bank would be a warehouse for those funds deposited by its customers, and they would own the deposits, not the banks, and the banks would hold those deposits in trust for those customers.

I think that that is true.

Mr. Goldsborough. But that is not involved in this bill of mine.

Mr. Brougham. That is not involved in your bill. This bill would permit the banks to function precisely as they do now, owning their deposits.

Mr. Williams. Of course, that is true; but what we were talking about was increasing the reserves to 100 percent. As I understood the purpose of this bill, you would finally reach that point.

Mr. Goldsborough. That is not the purpose. It might result in that.

Mr. Brougham. It would be incidental.

Mr. Williams. What I was talking about, and what I wanted to have understood, if we can, is what this 100 percent means. As I understand Mr. Goldsborough, he said yesterday that the loans of the bank could be made against that reserve. Do you subscribe to that?

Mr. **Brougham**. According to the set-up of this bill, yes.

Mr. **Williams**. This bill or any other, if you have a 100-percent reserve. Take this bill and assume that it would result in a 100-percent reserve——

Mr. **Brougham**. Under the accepted Fisher plan——

Mr. **Goldsborough**. Just leave the Fisher plan out.

Mr. **Brougham**. All right. The banks could loan exactly the same as they do now.

Mr. **Williams**. How, if they got a 100-percent reserve? What is a reserve?

Mr. **Brougham**. A reserve in this case would be——

Mr. **Williams**. In any case.

Mr. **Brougham**. Of course, we are considering the set-up of this bill.

Mr. **Williams**. All bank reserves, let us say.

Mr. **Brougham**. Shall we take the case of the reserves now?

Mr. **Williams**. Yes.

Mr. **Brougham**. The reserves now are such that the banks can lend five times the reserves, and can manufacture five times the amount of book credits and lend them out.

Mr. **Williams**. Is it your idea that loans are made in accordance with the reserves?

Mr. **Brougham**. Certainly. That is the only way a bank will lend.

Mr. **Williams**. And the more reserves that you have——

Mr. **Brougham** (interposing). The more the bank can expand on those reserves——

Mr. **Goldsborough**. That is subject to correction.

Mr. **Brougham**. According to the fractional reserve system.

Mr. **Williams**. The more reserves you have the more you can expand?

Mr. **Brougham**. Yes.

Mr. **Williams**. What relation have the reserves to the deposits?

Mr. **Brougham**. The reserves have no relation to the deposits. The loans have a direct relation to the deposits.

Mr. **Goldsborough**. The deposits correspond to the loans——

Mr. **Williams**. Wait a minute. Is it not a fact that the reserves under our present system are based upon the amount of demand deposits?

Mr. **Brougham**. No, sir. The amount of demand deposits is based upon the reserves.

Mr. **Williams**. What is it that determines the amount the banks shall now put up as reserves under our present law, 10 percent or 20 percent? Fourteen, 20, and 30 is the ratio now, I think.

Mr. **Brougham**. Yes; 14, 20, or 30 of the amount which they lend.

Mr. **Williams**. What determines how much that amount shall be, as a reserve? Is it not based upon the amount of your bank deposits?

Mr. **Goldsborough**. No——

Mr. **Williams**. Wait a minute. Isn't that a fact?

Mr. **Brougham**. No. The deposits are really based on the loans, that is, every loan creates a deposit.

Mr. **Williams**. Of course, your deposits are so much in a bank, and——

Mr. Brougham. Now a bank's loans are based upon the deposits.

Mr. Williams. The deposits are based upon the loans?

Mr. Brougham. I mean, upon the reserves. The bank's loans are based upon the reserves. The deposits are determined according to the amount the bank lends.

Mr. Williams. The reserves are determined by the amount of deposits that are on the bank's books, whether it is in loans or cash.

Mr. Brougham. The bank creates those deposits, as a rule, by lending book credits.

Mr. Williams. All right. That is a deposit.

Mr. Ford. Just a part of it.

Mr. Brougham. Let us say about 95 or 97 percent.

Mr. Ford. I do not agree with that.

Mr. Williams. All right. Whatever it is, that is a deposit in the bank, whether it is the result of a loan or deposit or cash.

Mr. Brougham. Yes.

Mr. Williams. That is a deposit in that bank.

Mr. Brougham. Yes.

Mr. Williams. It is a liability of the bank.

Mr. Brougham. Yes, sir.

Mr. Williams. Now, isn't that the thing that determine the amount of reserves that that bank must carry with the Federal Reserve? Isn't it?

Mr. Ford. Under present law.

Mr. Brougham. Under existing law, the bank cannot loan beyond a certain ratio of the reserves.

Mr. Goldsborough. I can straighten that out.

Mr. Williams. I want this man to straighten it out, if he can.

Mr. Goldsborough. It does not make any difference who straightens it out.

Mr. Williams. Do you say that that is not the thing that determines the amount of reserves that the bank carries with the Federal Reserve System, the member bank?

Mr. Brougham. No. The bank must have a base, usually its capital and surplus, and on that base it can loan a multiple of the reserves. Now, according as it lends, it creates deposits, new money, new bank money, which circulates until the loans are called. If it is a short-term loan, it will circulate for 90 days. If it is a long-term loan, it will circulate until that is paid.

Mr. Williams. You say that the deposits do not determine the amount of the reserves?

Mr. Brougham. No.

Mr. Spence. Let me ask you a hypothetical question. Suppose that the reserves are 10 percent. How much could the bank lend—how many times the amount of the reserves could the bank lend?

Mr. Brougham. Ten times.

Mr. Spence. And if the fractional reserve was 25 percent, it could lend four times?

Mr. Brougham. That is right.

Mr. Spence. And if the fractional reserve is 50 percent, it could lend one time?

Mr. Brougham. Twice.

Mr. Spence. That is correct; is it not?

Mr. Brougham. It could lend twice.

Mr. Spence. That is right; two times. But if the fractional reserve was 100 percent——

Mr. Brougham. Then it could lend once.

Mr. Spence. How could it lend once?

Mr. Brougham. It could lend what it has got.

Mr. Spence. It could not lend on its reserves?

Mr. Brougham. Certainly, a bank can lend its reserves. It draws down its reserves as it lends that.

Mr. Spence. Would there be anything to lend except its capital and surplus?

Mr. Brougham. If cash were deposited in the bank, if the new money were deposited in the bank, that is reserve money, and it could lend that, and it would own it—that is, if the depositor deposited it in cash in the bank, the bank would immediately own the cash and it would exchange for that cash an obligation to pay upon demand the amount of it.

Mr. Spence. The reserves are based not only upon cash deposited, but upon the amount on the books of the bank as deposits.

Mr. Brougham. Not as I understand it.

Mr. Spence. What are they based on?

Mr. Brougham. I think I stated correctly the situation, that——

Mr. Goldsborough. Mr. Brougham, I think that I can straighten this out.

Let us assume that a bank has a capital stock, at its inception, of $100,000. That capital stock can be used for the purpose of loaning a million dollars, can it not?

Mr. Brougham. Yes.

Mr. Goldsborough. Suppose that a bank accumulates a surplus of another $100,000. It could then loan $2,000,000, could it not?

Mr. Brougham. Yes.

Mr. Goldsborough. Let us suppose that the customers come into the bank, which of course they never do unless there is a run on the bank, but let us suppose that a number of customers come into the bank and they withdraw in cash $100,000. Even though the bank at that time still has a capital of $100,000, and a surplus of $100,000, as its cash reserve has been reduced by $100,000, the reserve would then be said by the bank examiners to be impaired——

Mr. Brougham. By $100,000.

Mr. Goldsborough. And they would immediately require the bank, under our present system, to collect $1,000,000 of its outstanding obligations, in order to reestablish its reserve.

Mr. Brougham. Yes.

Mr. Goldsborough. That is correct, is it not?

Mr. Brougham. That is correct.

Mr. Ford. Now, let us see——

Mr. Goldsborough. Let me carry this through. Then we will all understand it, I think.

Mr. Ford. I cannot get it in my head.

Mr. Goldsborough. Now, let us assume that this discount goes into operation, and the discount goes into the hands of the retailer and he deposits it in the bank. It would increase the bank's cash reserves, would it not?

Mr. Brougham. It would.

Mr. Goldsborough. Then suppose that in view of the fact that the bank's cash reserves were increased, and that the Federal Reserve System increased reserve requirements accordingly so as to avoid any inflation of the currency, and suppose further that that condition continued until the Federal Reserve System required a 100-percent reserve, it would simply mean that the bank could either loan what it had in cash, or it could keep that cash in its reserve and loan the money by the same bookkeeping and checking process that it does now.

Mr. Brougham. Certainly. Book credits could be issued upon it to 100 percent.

Mr. Goldsborough. That is all that there is to it, gentlemen.

Mr. Williams. You get back, according to my view of it, to the amount of deposits in the bank, whether it is cash or credit deposits. That is a fact, is it not?

Mr. Brougham. You mean that credit deposits can serve as a reserve for the bank?

Mr. Williams. Not as a reserve, but as a base upon which the reserves are counted.

Mr. Brougham. You get the reserves first, and then you create your deposits with bank credits.

Mr. Goldsborough. The reserves come first.

Mr. Ford. Let me ask——

Mr. Williams. Let me finish.

Suppose that you have a bank with $500,000 in deposits and $500,000 in cash reserve, on 100 percent.

Mr. Brougham. Yes.

Mr. Williams. You have deposits there, and those are liabilities, are they not?

Mr. Brougham. Yes.

Mr. Williams. Whether they are in cash or in credits. Of course, you have the reserves equal to them.

Mr. Brougham. Yes.

Mr. Williams. Let us say that you make a $100,000 loan. What effect would that have on your credits? Let us take first $100,000 in loans made, and the cash is taken out.

Mr. Brougham. On that loan?

Mr. Williams. Yes. What shape is your bank in now?

Mr. Brougham. That draws down the reserves of the bank by $100,000, and if it is drawn below the limit of reserves, the bank examiner comes in and says——

Mr. Goldsborough. That is upon a 100-percent reserve?

Mr. Williams. Yes.

Mr. Brougham. All right.

Mr. Williams. You are below 100 percent.

Mr. Goldsborough. No.

Mr. Brougham. You are still on a 100-percent basis. You paid out to the man to whom you loaned the money, a part of the reserves.

Mr. Williams. What does 100 percent mean?

Mr. Brougham. It means you pay dollar for dollar.

Mr. Williams. Against your deposits?

Mr. Brougham. Against your deposits, yes sir. You pay dollar for dollar against each man's deposits. This man has drawn $100,000 in cash. You still have $900,000 left, to meet the demands of your other depositors.

Mr. **Williams**. But you still have $500,000 deposits.

Mr. **Brougham**. $400,000.

Mr. **Williams**. You still have $500,000 deposits.

Mr. **Brougham**. Not if he has withdrawn it.

Mr. **Transue**. Mr. Williams is talking about now?

Mr. **Williams**. Yes.

Mr. **Brougham**. You have loaned him that money, and he withdraws it in cash.

Mr. **Williams**. Let us suppose that he takes credit on the books.

Mr. **Brougham**. No addition?

Mr. **Williams**. No; not any addition. Suppose, instead of cash, he wants——

Mr. **Brougham** (interposing). Oh, credit? That is all right. That is cashable at any time. The bank has the cash behind it.

Mr. **Williams**. Does not that create an additional $100,000 deposit?

Mr. **Brougham**. No; no.

Mr. **Williams**. And a liability?

Mr. **Brougham**. No. The bank holds in idle funds, in idle cash, $100,000 which he has not withdrawn, and it is on a 100-percent reserve.

Mr. **Williams**. He has not the cash, but he has the credit?

Mr. **Brougham**. He has the credit, and he uses that.

Mr. **Williams**. But that is an obligation of the bank, is it not?

Mr. **Brougham**. That is an obligation of the bank.

Mr. **Williams**. Your obligations are now, say, $600,000.

Mr. **Brougham**. No.

Mr. **Ford**. Your cash obligations are $600,000. Your gross obligations are $500,000, plus this man's security.

Mr. **Goldsborough**. Your obligations are just what they were before, on a 100-percent basis.

Mr. **Williams**. But you created an obligation to pay him on your books an additional $100,000.

Mr. **Brougham**. But he has taken it in credit, and you have not paid him out of your reserves.

Mr. **Williams**. But it is at the same time a deposit.

Mr. **Brougham**. It is a deposit; yes.

Mr. **Williams**. And it is a liability of the bank.

Mr. **Brougham**. It is a liability of the bank that is not called.

Mr. **Williams**. After that transaction, it would make the liabilities of the bank, instead of $500,000, $600,000?

Mr. **Brougham**. I think not. I think the bank has the same liabilities it had before. The point is that the man, if he takes it out in credit, has not asked the bank yet to pay its obligation to him.

Mr. **Williams**. He has not asked them to do it, but it is an obligation of the bank.

Mr. **Brougham**. Yes; but it is the same obligation that the bank today pays.

Mr. **Williams**. And your deposit liabilities are $600,000?

Mr. **Brougham**. Not under a 100-percent reserve.

Mr. **Williams**. Well, if it is not, I do not want to create a liability, if that is not one of them.

Mr. **Goldsborough**. The cash has not been reduced by that amount.

Mr. **Brougham**. It is either reduced or held idle.

Mr. Goldsborough. What you are actually loaning him on a 100-percent reserve is the cash itself. Your bookkeeping calls it a reserve in order to keep the bank running as it is now.

Mr. Spence. Your idea is that when you transfer the deposits to loans, that reduces the amount of the reserves?

Mr. Brougham. You do not transfer deposits to loans. You never loan another man's deposit which is held on demand.

Mr. Spence. As you loan the money of the bank, that which the bank is debtor on to the depositor, does that reduce the reserves, as you make the loans, according to your theory, or the reserve requirements?

Mr. Brougham. The obligations of the bank would be cash obligations; that is, under the 100-percent reserve set-up.

Mr. Spence. And as you made the loans, you would reduce the requirements for reserves? Is that it? Would the reserves be reduced in the amount of the loans that you make?

Mr. Brougham. Either the bank would pay out the cash or hold the cash idle, subject to the demand of the depositor.

Mr. Spence. Therefore that would reduce the reserves to that extent?

Mr. Brougham. It would reduce the amount of the reserves, and the reserves would still be 100 percent against the other remaining obligations.

Mr. Ford. Would it not clarify the situation if somebody made up a chart and gave us a typical set-up of that in chart form?

Mr. Goldsborough. Probably we can do that tomorrow.

Mr. Ford. You made a statement the other day in which you said that you would like to have somebody think it over; you said this—that the banks were busted in 1933, and that the Government borrowed a certain amount of money——

Mr. Goldsborough. From the banks.

Mr. Ford. All right. Let us take that. The banks were broke, but the Treasury borrowed from the banks 3½ or 4 billion dollars, or whatever it was, from busted banks which had no money. The Treasury borrowed that from the banks at 2¾ percent, to use a normal figure. Then the Government backed the R. F. C. notes for that amount, at 3 percent. Then the R. F. C. loaned that back to the banks at 3½ percent—isn't that about what happened?

Mr. Goldsborough. That is about what happened, but I abbreviated it to make it more graphic.

Mr. Ford. What happened was that the banking system of the United States, which was broke, loaned to the Treasury of the United States—let us say it was a billion dollars, for convenience—a billion dollars at 2¾ percent. Then the Treasury loaned to the R. F. C. that billion dollars at 3 percent, giving them a quarter percent margin. Then the R. F. C. turned around and loaned that money, which did not exist originally, to the banks at 3½ percent.

Now, the Treasury took that and paid 2¾ percent. The R. F. C. got it for 3 percent, and the R. F. C. loaned the money back to the banks, or took their stock at 3½ percent, and I want to ask this simple question: Was that a Houdini operation?

Mr. Goldsborough. Of course, I do not think that Houdini, as skillful as he was, could ever perform gymnastics the way the Treasury performs them. If everybody in this room were to chain Houdini completely and lock the chains and throw him in Chesapeake Bay, he would come up in 3 minutes without a thing on him, but that does not begin to touch what can be done with our system of financing.

Mr. **Ford**. But isn't that the actual situation?

Mr. **Goldsborough**. Yes, sir. These banks were actually busted, and yet the Federal Government borrowed the money from busted banks and loaned it back to the same busted banks in order to reestablish them and put them on a sound foundation.

Mr. **Transue**. Let me ask you——

Mr. **Goldsborough**. In other words, they did what could not be done.

Mr. **Meeks**. It can be done.

Mr. **Ford**. It was done.

Mr. **Transue**. Let me ask you this: Were the ones who furnished the money to the Treasury and to the R. F. C. busted at the time they furnished that money to the Treasury and the R. F. C.?

Mr. **Goldsborough**. Do you mean the banks?

Mr. **Transue**. Those banks that furnished the money.

Mr. **Goldsborough**. Absolutely.

Mr. **Transue**. Do you mean that all the banks——

Mr. **Goldsborough**. I do not mean to say that their doors had been closed, but I do wish to say that an artificial valuation, which did not exist, was placed on the securities in order to keep the doors open, so that they were busted, in fact.

Mr. **Brougham**. This was a measure of rehabilitation of the banking system, so that they would not have to close their doors. In addition, the Government went ahead and borrowed from the banks more than they ever had, and it still is borrowing more than they have got, without touching what they have got. It has borrowed something like $10,000,000,000 during the Roosevelt administration, and I think they have on their books now between fourteen and fifteen billion dollars of Government obligations without ever touching their stockholders.

Mr. **Transue**. I would like to have you tell me this——

Mr. **Brougham**. They did it on this pyramiding.

Mr. **Ford**. Was that pyramiding of banks, or was it actually that many banks that subscribed to those loans from the Treasury knew before they subscribed that they could not turn them out to their customers and get that money?

Mr. **Brougham**. They knew that they could manufacture the money themselves, and they did not want to turn them out to their customers.

Mr. **Ford**. You do not want to tell me that that money that was borrowed by the Government went to the banks?

Mr. **Brougham**. Half of it did.

Mr. **Ford**. That is all right, but there was the push of one-half that came from individuals.

Mr. **Brougham**. Just listen to what Governor Eccles said about this:

> In purchasing offerings of Government bonds, the banking system as a whole creates new money or bank deposits. When the banks buy a billion dollars of Government bonds as they are offered—and you have to consider the banking system as a whole, as a unit—the banks credit the deposit account of the Treasury with a billion dollars. They debit their Government-bond account a billion dollars, or they actually create, by a bookkeeping entry, a billion dollars.

It was the reliance upon their ability to create that money that has allowed all of this Government financing to take place.

Mr. **Ford**. I happen to know that when California institutions will subscribe for a Government loan, they will subscribe for about three times what they expect to get.

Mr. **Brougham**. Maybe a dozen times, because they want to get a larger apportionment provided so that they can create the money for it.

Mr. **Ford**. They do that because they know that the moment their allotment is made they can hand those bonds right over the counter and sell as many of them as they want to, because there are literally billions of dollars in the country owned by individuals who want to put that money into tax-exempt securities. That is true, is it not?

Mr. **Brougham**. But the reason they oversubscribe so much and so extravagantly is that they are able to create this money out of hand, and the more they can create the more they are drawing interest.

Mr. **Transue**. You mean that they just make money by making bookkeeping transactions?

Mr. **Brougham**. That is precisely what Governor Eccles said. I just quoted him.

Mr. **Goldsborough**. Yes. If they get the Federal Government to borrow $100,000,000 from the Chase National Bank, this is what happens: The Government carries the bonds to the Chase National Bank and hands them over, and some $25-a-week clerk puts on the books of the Chase National Bank $100,000,000 less discount. That is all that happens. The Government first borrows the money from the bank and then, by redepositing it, loans it back to the bank and proceeds to pay interest.

Mr. **Williams**. The Government borrows money just the same as an individual.

Mr. **Brougham**. The Government borrows money just the same as an individual.

Mr. **Williams**. The transaction between the bank and the Government is exactly the same as it is between an individual and——

Mr. **Brougham** (interposing). Precisely. It is a creation of new money.

Mr. **Ford**. Suppose that I am good for $10,000, which I am not, but I go into the bank and say to the manager or the cashier, "I want to borrow $10,000," and he makes an inquiry to find out what I want it for, and I assure him that I want to use it the right way, and that I have the ability to pay it back. He gives me credit on his books for $10,000.

Now, what appens? The deposit liability of that bank is immediately increased $10,000, is it not?

Mr. **Brougham**. Yes.

Mr. **Ford**. I have put up, supposedly, sufficient security to cover my loan.

Mr. **Brougham**. Usually more than the amount of the loan.

Mr. **Ford**. Then the credit and the debit are balanced, are they not, assuming that my security is good?

Well, let us assume that he said "All right." I do along, and in the course of the next 2 or 3 months I check out that $10,000, and I am building a house, we will say, and I build it, and it is all completed, and within the 90-day period I sell it and I get paid for the house $10,000 or whatever I sell it for and go back and pay my debt to the bank.

Mr. **Brougham**. Yes.

Mr. **Ford**. What happens? I create $10,000 of new money, or did the security that I gave to the bank create the $10,000, or did the bank create it?

Mr. **Brougham**. The bank, with your permission, and with the security which you put up, manufactured some new money which went out of existence when you paid the bank, when you paid your loan. If the bank does not reissue it as a new loan, the general money system is without the $10,000. If it had been reissued, it would have remained in the system and been turned over as consumer income twice or three times a year, according to whether we have good times or bad times, but now it is blotted out of existence.

Mr. **Goldsborough**. I want to approach this from another angle, because I believe this 100-percent reserve is just as simple as it can be, if we can just get the idea. I think some of the members of this committee are confusing loans with deposits.

I think it was stated a few minutes ago that under a 100-percent reserve system you could loan the amount of your deposits. That never has been the condition. There is no relationship between the amount you could loan and your deposits. What you can loan under a 100-percent reserve is the amount of your reserve, which is equal to cash.

That is correct, is it not?

Mr. **Brougham**. That is right.

Mr. **Goldsborough**. If your reserves, which would be your cash, amounts to $500,000, you could keep your loans up to $500,000, and you could not pass the $500,000 at any time. You would be confined in your loaning operations to the $500,000, regardless of what your deposits are.

That is correct, is it not?

Mr. **Brougham**. Yes.

Mr. **Goldsborough**. That is all that there is to it.

Mr. **Ford**. You take another example——

Mr. **Goldsborough**. That one covers it.

Mr. **Transue**. May I interrupt there?

Mr. **Goldsborough**. Certainly.

Mr. **Transue**. Then, in the country over, and in the banking system in general, the amount of loans that the banks could make would be limited to the amount of cash the Government has issued?

Mr. **Goldsborough**. The amount of cash in the banking system.

Mr. **Transue**. Which would be about that amount?

Mr. **Goldsborough**. What amount?

Mr. **Transue**. The amount issued by the Government.

Mr. **Goldsborough**. Under the operation of this particular bill, it would be the amount approximately of the retail discount, less about 10 percent.

Mr. **Ford**. Then you are going to scrap entirely what we call the self-liquidating principle.

Mr. **Goldsborough**. I do not know about that. If the time should ever arrive——

Mr. **Ford**. With 100 percent reserves, you would absolutely scrap what we know as the self-liquidating principle.

Mr. **Goldsborough**. But there is nothing in this bill which requires a 100-percent reserve.

Mr. Ford. I know, but we are talking about that right now, whether it is in the bill or not. Let us think of this: Somebody has suggested that we build a series of roads across the continent, expending a huge sum, $8,000,000,000. Now, we cannot build those roads because $8,000,000,000 is not immediately available to anybody to build them with, but we think the country is going ahead and that the amount of travel on those roads over a period of 20 years will liquidate that amount by charging a small toll charge to everybody who travels on those roads.

Now, if the 100-percent reserve is going to stand, the only amount that we could loan in order to build those roads at any time would be the equivalent of whatever reserves are available in the country at that time. There are, I understand, $1,143,000,000 of reserves at the present time. Multiply that by 10 percent, and that would be $10,000,000,000. If $8,000,000,000 of that were made available for the building of roads, there would only be $2,000,000,000 for other business.

Mr. Goldsborough. Suppose that that did happen; all that the Federal Reserve System would have to do, if they wanted to make those 8 billions available, would be to reduce the reserve requirements. After they get up to 100 percent, that does not mean that they have to stay there.

Mr. Ford. If 100 percent is the ideal condition, why shouldn't they stay there?

Mr. Goldsborough. I understood you to say that that would be a detriment, because they could not do it, and I do not think it would be a detriment, but if it were they could get the $8,000,000,000 by reducing the banks' reserves.

Mr. Ford. I just want to make this observation——

Mr. Goldsborough. But personally I think we ought to get the money before we build the roads.

Mr. Ford. Then we would not build them, but I want to make this observation, and make it seriously, that on the basis of the 100-percent reserves in the banks, it would be, in my judgment, the most deflationary proposal that has ever been made to the Congress or anybody else with reference to the expansion of American business. Now, I may be wrong——

Mr. Brougham. May I make a statement on that?

Mr. Goldsborough. Certainly.

Mr. Brougham. Let us suppose that under this bill the people of the country—let us personify them, and call them the American people—called the retailers together, and they said:

> Now, we are buying so much of you every year, and we have a 20-percent margin of productive power, as producers, which we are not using with our existing equipment and with our existing labor which is unemployed. We will make a bargain with you. We will still continue to buy that 80 percent of you, but we want to buy of you 20 percent more, and we will provide the means to do it. We will give you a draft upon our labor and upon our productive power of that 20 percent extra. We will do that not as individuals, but as the whole people.

Somebody asked me the other day who would hold the bag, and I said the whole people, with its productive power, both used and unused.

The people would go on and say:

> We will arrange it so that you will sell to us 20 percent more goods, and the individuals who buy those goods will pay just the same sum as they are paying now, but we will make up that 20 percent to you in new money, in new circulating bank deposits which will be put upon that extra 20 percent of our productive ability which is now being wasted and unused. Now we are validating that money with this unused productive capacity which we are willing to hand to you, to be used by you in your increased orders back to the wholesalers, and in the wholesalers' increased orders back to the manufacturers, and in the increased orders from the manufacturers to the prime producers—and we are paying for the new money with our labor and with our productive power.

Now, there is no borrowing of private groups there. There is new money, which we, as the American people, are giving to these retailers in excess of what we individually had been giving to them, and on which they can claim our added labor and claim added goods; and that money will go on circulating for our labor and goods, and it is perfectly good money, because it has back of it the formerly unused capacity which will then be in use.

Now, what will happen? We will not borrow of the National City Bank or anybody, or sell any bonds to them at all. We have manufactured that money just as they do manufacture it and lend it to us, only we do not have to pay any debt for it except with our goods and services, and the retailers will find that our goods and services, in the extra margin, are available to them when they bring that new money into the market.

Mr. Ford. I think I understand that perfectly. I see that very clearly. But I am just thinking of this situation, that the average manufacturer is in the business of manufacturing for the purpose of getting his costs, plus a profit, and I can readily see that that profit might be in the 15-percent discount that he has offered on his prices, when we cut them, and I am talking about Mr. Goldsborough's bill, the 15-percent discount——

Mr. Brougham. That is a 20-percent increase in purchasing power.

Mr. Ford. But we will make it a 15-percent discount. He takes his deposit at the end of the day or week, and goes to the bank and deposits, we will say, $850, and he gets credit on the books of the bank for $1,000. Then the bank in turn debits the Treasury for $150, does it not?

Mr. Brougham. That is true.

Mr. Ford. And the Treasury in turn sends him the currency, or credits it on their books for interbank-currency purposes in the sum of $150. When you multiply that figure by the gross business of the country, it runs into billions. I think it is 1 billion 500 million in the course of a month.

Mr. Brougham. Yes; of new goods sold.

Mr. Ford. What the Treasury has done, then, is to make good the difference between the retail price the thing was sold for, and what they actually got to make that up, and put that in the bank's vault, and the bank used it for a reserve, and I can conceive of a situation where over the course of 6, 9, or 12 months all of the banks' reserves would consist of interbank currency, assuming that they went on in their normal way and made the usual loans and balanced the loans with their reserves, and all that.

So at the end of the year there is a deficit against the Treasury of, we will say, 10 or 15 billion dollars; we will use the figure of 15 billion dollars.

Now, then, the banks want to make some more loans. What the banks can loan is then the absolute equivalent of the amount of interbank currency that they have in their reserves. That will limit those loans from then on, and the loans will be on a 100-percent basis.

Don't you agree with me that when that condition comes about, the normal capacity of the bank to loan will immediately be cut down from three, four, or five times, as it is doing now, to one time?

Mr. **Brougham.** But the amount of money has increased correspondingly.

Mr. **Ford.** But that money is not in circulation. It is in the banks. If it were possible for the banks to make that money available in the usual way, I would say that you increased the amount of money, but when you limit it to just one for one, I think—and I may be wrong—that you are immediately restricting credit——

Mr. **Brougham.** Now, Mr. Ford, a little while ago you were expressing fears that this would mean unlimited inflation, and you say here that it would mean unlimited deflation.

Mr. **Ford.** I used the term "deflation," and that is what the situation would bring itself to. We would have 15,000 banks in the United States with reserves of——

Mr. **Goldsborough.** $60,000,000,000.

Mr. **Ford.** No; they would not have that much.

Mr. **Goldsborough.** Why not?

Mr. **Brougham.** Why not?

Mr. **Ford.** Because the reserves are limited to the amount of money put into the interbank currency.

Mr. **Goldsborough.** We did not say anything like that.

Mr. **Brougham.** You may be supposing that, but it is not so.

Mr. **Goldsborough.** There is not a word in the bill to justify a conclusion of that kind. What the bill says is that if this interbank currency should increase from time to time, the Federal Reserve System could increase reserve requirements.

Mr. **Ford.** They would, naturally.

Mr. **Goldsborough.** I know, but the Federal Reserve Board is not going to increase reserve requirements unless it is necessary.

Mr. **Ford.** Do we know that?

Mr. **Goldsborough.** They are not supposed to. They would have the same authority to do it that they have now.

Mr. **Ford.** Here is a bank that has loaned all of its normal reserves to the limit, and it has in its reserve at the present time $1,000,000 of interbank currency.

Mr. **Goldsborough.** Mr. Ford, let us understand that the Federal Reserve would not be supposed to increase the reserves to that extent unless and until there was enough interbank currency in he banks to take the place of the fractional reserves which had previously been used.

Mr. **Ford.** If 15 billion dollars of interbank currency went into our circulating currency, that is all of the reserves that they would have.

Mr. **Goldsborough.** No, indeed.

Mr. **Brougham.** No. That would be added to the present reserves.

Mr. Ford. The principle of the bill is to ultimately put interbank currency into the banks for reserve purposes.

Mr. Brougham. And, in addition——

Mr. Ford. Whenever that happens, then the lending power of the banks of the country is limited exactly to what their reserves are, on a 100-percent basis.

Mr. Goldsborough. Then the reserves would probably be 60 or 70 billion dollars.

Mr. Ford. I do not see how that could be.

Mr. Brougham. There is a mandate in this bill to prevent deflation on the part of the Federal Reserve Board.

Mr. Ford. Then I do not understand the bill.

Mr. Goldsborough. It is perfectly simple, Mr. Ford.

Mr. Ford. It is too damned simple.

Mr. Goldsborough. No, no! there is no use to have a misunderstanding about a perfectly simple matter. There is no requirement in this bill, Mr. Ford, for the Federal Reserve Board to increase reserves at all. They do not have to do that under the bill. They are given the power to do it, if they find that so much money is getting into circulation that it is necessary to do it in order to avoid inflation.

Suppose that the Federal Reserve Board reached the conclusion that we should have in circulation 60 billion dollars. What they would do is this: As this interbank currency went into circulation, their attempt would be to increase the reserve requirements in order to keep the circulating media at or about 60 billion dollars, and they would not increase their reserves except to the extent necessary in order to avoid the circulating media going beyond that point.

Mr. Ford. How do we know they would not?

Mr. Goldsborough. That is what this bill says.

Mr. Ford. How do we know they would not?

Mr. Goldsborough. We have to assume that they know how to attend to their business, just like they are doing it now. We have given them the right now to increase reserves 100 percent, on the theory that they know what they are doing.

Mr. Brougham. In addition, there is the mandate in the bill to prevent inflation and to prevent deflation.

Mr. Ford. I do not know. I have gone into this thing, and have gone over it thoroughly, but I do not presume to have a monumental mind.

Mr. Goldsborough. But I think that you understand the bill. You see, Mr. Ford——

Mr. Ford. Let me make this statement clear. If I thought that this bill would give the American people an additional 15 percent purchasing power, without in the end restricting the Nation's ability to carry on, and that it would provide the necessary money to carry on the increase in purchasing power and increase the consumption up to the point where it would absorb our productive power, putting the country on an equal basis as to production and consumption, so that everybody would be able to have a job and everybody would be able to buy the commodities that others produce and that it would leave a reasonable margin for the people making these goods so that they could pay their taxes and other normal obligations, and carry on, I would be for it, wildly and enthusiastically.

Mr. Goldsborough. Everybody else would.

Mr. Ford. Yes; but it seems to me that you have done one thing. You have done exactly what we do in any national law that we pass. You can always punch a hole in a pillow, can't you, by shoving your hand in it?

Mr. Goldsborough. I don't know. I never got that drunk.

Mr. Ford. But the trouble is, while the hole is your objective, on the other end of the pillow it pushes out, and where you made a depression on one side you make an expansion on the other, and I am afraid that that will be the result of this bill, unless this interbank currency is actually validated as real money in the general circulating system.

Mr. Brougham. But, Mr. Ford, it is validated in the form of demand bank deposits.

Mr. Goldsborough. The bank can use it as it would ordinary bank deposits, but they can only use it once under this bill.

Mr. Ford. If they can only use it once you have restricted the credit possibilities.

Mr. Goldsborough. No; they can still use the money they now have, which is not interbank currency, for fractional reserves. It does not interfere with their present operations at all, and it was deliberately framed so that it should not interfere with the present operations.

Mr. Ford. I appreciate that you tried to frame it so that it would not, but in my understanding of it it will.

Mr. Goldsborough. But it won't. Suppose that a bank has on deposit $8 in the usual way and $2 of this interbank currency. It can use the $8 for the fractional reserve. It can expand that and make $80 out of it for loaning purposes, but the $2 it can only loan once. If in the course of time the expansion of the interbank currency becomes so great that the loaning of it once is sufficient to transact the business of the country then there is no necessity for having a fractional reserve, but under this bill the Federal Reserve Board not only has the right to increase reserves but it also has the right to decrease reserves, and if a deflationary condition such as you have in mind should come about the Federal Reserve Board can immediately decrease reserve requirements.

Mr. Ford. Would it not be possible that in that decrease they might have to include the interbank currency's expansion power?

Mr. Goldsborough. Of course, if in 10 years from now we should reach that point——

Mr. Ford. I am not speaking of that.

Mr. Goldsborough. Just 1 minute. We could have further legislation then, but there is no necessity to anticipate that at this time. A bill could be passed changing interbank currency into real currency in 1 day if the time ever came when it was necessary to do it.

Mr. Ford. And we could pass a bill today just simply telling the Treasury that we needed $40,000,000,000, and they could issue it.

Mr. Goldsborough. That is not the purpose of this legislation.

Mr. Brougham. Mr. Ford raised a question about that $8,000,000,000 for highway projects, and I would like to show him how, under this proposal, the projects could be put through without its costing the taxpayers of the United States anything except——

Mr. Ford. When you talk about a project of that kind, which is a physical project, not costing anybody anything, I think that you are just simply talking in the wind.

Mr. Brougham. I mean that it is costing the country fully that now in what it wastes in unused capacity. Let us suppose that under this bill there has been issued $10,000,000,000 of interbank currency, and it is decided not to have a 15-percent discount, but 3 percent. That would free eight billions of this interbank currency to build those roads, and it would employ men, and it would use the materials and the labor, now wasted in this country, in building those roads; and you would find that the roads were paid for at the time they were built and that we would have the roads and, besides, have made a net gain in the standard of living of a little over 3 percent instead of 20 percent.

Mr. Ford. Somebody would have to make that up. This is getting money out of the blue sky.

Mr. Brougham. It is not getting money out of the blue sky. It is money out of capacity now wasted and going over the dam and doing nobody any good, and we are trying to salvage that, and that is not getting money out of the blue sky, but on earth and above the ground.

Mr. Luce. Mr. Brougham, from the days of the bartering stage it has generally been accepted that purchasing power results from and corresponds to a mass productive power.

Mr. Brougham. Yes, sir; I subscribe to that heartily.

Mr. Luce. I understand your view to be that there is idle and not effective productive power now.

Mr. Brougham. To a very considerable extent. We see it in millions of unemployed and in the wheels of factories that are half employed all the time.

Mr. Luce. Various proposals have been laid before the public in order to meet this situation, among them one by Dr. Townsend.

Mr. Brougham. Yes; I am familiar with it.

Mr. Luce. Dr. Townsend originally proposed that $200 a month be put into the hands of the elderly persons of the country to accomplish this same purpose. Isn't that what is contemplated here?

Mr. Brougham. Yes; it is like it. I have only a quarrel with the means with which he would accomplish the purpose.

Mr. Luce. And there are other proposals of the same sort.

Mr. Brougham. Bushels of them.

Mr. Luce. I want to tell you frankly that I have had great difficulty in putting my finger on the weak spot in the Townsend plan, as I have great difficulty in putting it on the weak spot in this plan.

Mr. Brougham. I could help you put your finger on the weak spot in that plan; but I have tried very hard for several years to put my finger on the weak spot in this one, and I thought that there was a catch in it somewhere. I was brought up according to the straightest economic principles of Yale University, and I had a lot to unlearn before I gave up some of the things that I once accepted as beyond question.

Mr. Luce. I was only going to try to do it.

Mr. Brougham. All right, sir.

Mr. Luce. Perhaps we will save time by putting into the record my own version, and, frankly, it is by the use of the familiar process of reductio ad absurdum.

Mr. **Brougham.** Yes.

Mr. **Luce.** If we put $200 into the hands of those elderly people each month, would it not be twice as helpful to put $400 a month into their hands?

Mr. **Brougham.** Possibly.

Mr. **Luce.** And if it is wise to put it in the hands of persons over 65, would it not be still better to put it in the hands of persons over 50?

Mr. **Brougham.** I do not quarrel with that, for the sake of the illustration.

Mr. **Luce.** Now, going right straight down, in your plan, or Mr. Goldsborough's plan, you contemplate putting into the hands of the public, without any effort in return, 15 percent. Would it not be very much better to make it 30 percent?

Mr. **Brougham.** Wait a minute. You say without any effort in return. A few minutes ago I was calling in the retailers and saying to them that we are willing and anxious to produce 20 percent more. We are only able to buy from them what we are buying now, when we have these idle factories and idle hands, but we are willing to produce 20 percent more, and we will give them a draft upon us for goods and services to the extent of 20 percent more.

That is not without extra effort on our part. It is with extra effort on our part, and we put in what it takes.

Mr. **Luce.** Let us branch off to another aspect of the situation. The President said yesterday—and I have not read it beyond a brief reference to it in last night's paper, but if I understand it aright, the President proposes that we raise prices still more. Now, then, the President accepts the theory, evidently——

Mr. **Goldsborough** (interposing). I wonder if he means prices at retail. I do not think he does.

Mr. **Luce.** The President accepts the theory, evidently, that the volume of currency determines its value, or the quantitative theory of money. Do you accept that theory?

Mr. **Brougham.** I accept it in the main; yes, sir.

Mr. **Luce.** If we increase the number of pieces of paper, no matter what their shape, by 15 percent, if you accept the quantitative theory, you assume that the purchasing power of each one of those pieces of paper falls in value?

Mr. **Brougham.** That is not a statement of the quantitative theory. If you increase the quantity of paper without increasing industrial production at the same time, then it falls in purchasing power, but if you increase the production correspondingly with your increase in the volume of paper, the price level remains the same.

Mr. **Luce.** Is that what happened in Germany?

Mr. **Brougham.** No; because they increased the paper without increasing the production concurrently.

Mr. **Goldsborough.** They did it deliberately.

Mr. **Brougham.** They did it deliberately as a matter of repudiation of their domestic debt and as a matter of repudiation of their obligations to the Allies.

Mr. **Luce.** I cite that as simply one of many illustrations.

Mr. **Brougham.** That is inflation, but what we are seeking is not inflation, but a simultaneous increase in production corresponding to the increase in the amount of money, and that is not inflation.

Mr. **Luce**. Does not the Townsend plan contemplate precisely the same thing?

Mr. **Brougham**. You are radically wrong.

Mr. **Luce**. I would like to know why.

Mr. **Brougham**. The Townsend plan contemplates no increase in the productive capacity of this country, and it depends not upon an increase of money in the country; it depends upon taxing one class for the benefit of the elderly class.

Mr. **Luce**. Those are details.

Mr. **Brougham**. Those are details, but they are of the essence of the question.

Mr. **Luce**. I am getting down to the fundamental proposition with which we who doubt the Townsend plan are confronted every time we argue the question. We are told by the Townsend advocates, and there are many more of them than you suppose, that if we should put out money in this way we shall increase production.

Mr. **Brougham**. And they neglect the means whereby. That is a pious wish.

Mr. **Luce**. You have purchasing power in the hands of a multitude of people, many millions of people.

Mr. **Brougham**. You will transfer purchasing power from one class of persons to another class of persons, and you won't increase it in this country by the Townsend plan.

Mr. **Luce**. You cannot increase the purchasing power in this country as reflected in money without increasing the amount of money.

Mr. **Brougham**. Of course, I say that the taxing plan fails to increase purchasing power. This plan, of course, manifestly increases the purchasing power. None of the new money is given out until the retail price level is discounted to the consumers, and to the extent it is discounted, as they buy goods at the lower price their purchasing power is increased.

Mr. **Luce**. So is the purchasing power of the elderly class increased.

Mr. **Brougham**. The purchasing power of the elderly class is increased, but the men from whom that money was taken have their purchasing power correspondingly reduced. That scheme depends upon taxation. This scheme depends upon the creation of new money to balance hitherto unused productive material which it puts into the stream of consumer goods.

Mr. **Luce**. You have not increased purchasing power except by the symbols of it.

Mr. **Brougham**. I have increased purchasing power by the added production of the American people.

Mr. **Luce**. All of the Townsend people will tell you precisely the same thing.

Mr. **Brougham**. They will tell you, but we ask them for the means whereby. They say by taking it away from one class and putting it into the hands of the elderly people, and I say that you have not increased the purchasing power of the people by so doing.

Mr. **Luce**. Accepting your difference between the two plans, there still remains the fact that purchasing power has been increased under either plan.

Mr. **Brougham**. No, sir. Under the Townsend plan, I say that it is not increased one penny.

Mr. **Luce**. Simply a transfer?

Mr. **Brougham**. Simply a transfer by taxation of existing money and upon existing goods and services.

Mr. **Luce**. Do I understand that you think that under your plan there would be no artificial creation of wealth?

Mr. **Brougham**. No; there would be no artificial creation of wealth. The American people would say to the retailers, "We are ready to produce more; we are anxious; we have the men who are ready to go, but there is no employment for them. We are paying you so much for so much goods. We will pay you so much more, we—not individually but collectively; we will pay you the claims upon 20-percent more goods which we are ready to give to you the minute you present those claims, and that is in the added circulating bills, we will say"—and these added circulating bills, so long as they circulate, are paid for with new money attached to this new production, which production we are anxious and willing to provide. That does not mean that it is "without extra effort" on the part of the American people. They want to make the extra effort. They only want to know how.

Mr. **Luce**. You are speaking of new money?

Mr. **Brougham**. Yes.

Mr. **Goldsborough**. And the money does not come into being until the goods come into being.

Mr. **Brougham**. That is right.

Mr. **Luce**. That is just putting the cart before the horse.

Mr. **Brougham**. No; it is not. We have got the cart in the right place, behind the horse. The goods are sold at the discount, and the claims to the new goods are put into the hands of the merchants after they have performed their part of the bargain, to reimburse them, and we say, "Here are the goods right here in our idle equipment and in our idle labor, and just as soon as you increase your orders to the wholesalers, and then our men go to work and our wheels begin to turn——"

Mr. **Luce**. And that is a matter of weeks or months.

Mr. **Brougham**. That can happen very swiftly, and it is the only proposition now before the American people that will yank us out of our depression. We are in a bad fix right now. We have a depression that is going six times as fast as in 1929——

Mr. **Luce**. Now, Mr. Brougham, I am simply trying to find out what is representing the purchasing power in the interval between the 15-percent discount and the turning of the factory wheels.

Mr. **Brougham**. We will give them a month, and they will be repaid.

Mr. **Luce**. What happens in that month?

Mr. **Brougham**. That is the time when the act goes into effect, is it not?

Mr. **Luce**. My dear sir, after the act goes into effect——

Mr. **Brougham**. They have had a month's notice; Congress has passed this act, and you will find industry all set and ready to go then.

Mr. **Luce**. I am trying to foresee how it will happen; that is all.

Mr. **Brougham**. Yes.

Mr. **Luce**. In the interval between the 15-percent subsidy and the sale of goods over the counter?

Mr. Brougham. The sale of goods comes first.

Mr. Luce. I am talking about the productive process.

Mr. Brougham. We have existing inventories to draw upon, the goods on the retailers' shelves, the current that is in the powerhouses that goes into the homes that is drawn on 20 percent faster, which means that the orders for renewals go in 20 percent faster. That is all. The inventories are there already.

Mr. Ford. Would you allow me to make one tiny observation there?

Mr. Luce. Yes.

Mr. Ford. We have just observed the phenomena of a sudden drop in automobile purchases due to the fact that, for instance, a Chrysler Royal car that sold for $1,000, or $985, is suddenly boosted to, we will say, $1,100, or an increase of $115, and that happened all through the automobile industry, and the purchase of those cars immediately dropped off to an extent that the factories had to lay off a lot of people.

Now, possibly the increase was justified—I do not know—but I am satisfied in my own mind that if that $115 had not been added to the price of that car there would have been quite a number more of those cars sold, and I make that observation on my own experience. I contemplated buying one, but found that I would have to pay $115 more for it than I had to pay last year, so I thought that I would wait until next year, and that psychology applies to everything else. If this 15-percent discount had been in effect, that $1,000 car would have sold for $850, and the chances are that I would have bought one, and I presume that there are thousands of other people just in that same position.

Mr. Transue. Would not the company have gotten the profit of this 15 percent?

Mr. Ford. No.

Mr. Transue. On your argument, it would.

Mr. Ford. No. They would have gotten the original price of $1,000; but the retailer, who would make the normal discount when he sold the car, would only get $850 for it, but there would be a great many more cars sold on that basis. We cannot get away from the fact that there is something in this discount principle, but I think that the bill has been cluttered with one or two restrictions there that would seem to make it inoperative, and that is not particularly a criticism of the principle but merely a criticism of the present method of operation that is offered.

But I do not see any connection between this and the example you cite as far as the Townsend bill is concerned. I think the principles are absolutely reversed. One is taking from one class and giving it to another, and the class to which it is given is absolutely taken out of production. There is a distinction there, and I think that you [indicating Mr. Brougham] made a good statement on it. But the fact that those receiving the $200 a month are taken out of production, if they are not already out of production, is the difference, in my judgment, between that plan and the discount on an article, for by reason of the discount hundreds of more people will buy it, and therefore increase the consumption, and, naturally, by increasing the consumption you bring about a larger production.

Mr. **Luce**. You are absolutely right in saying it is different in the matter of putting other people out of production. I grant you that.

Mr. **Ford**. This, I am hoping, will put people in production, but maybe it won't. I don't know.

Mr. **Luce**. I share that hope, but I am trying to satisfy my fundamental conceptions of purchasing power with the program set forth in this bill, and I wish to point out that in the Townsend plan and in practically every other plan presented, there is the element of an increase of artificial purchasing power, which we know as inflation.

Mr. **Brougham**. Yes?

Mr. **Luce**. And I wanted to find out, and my questions were aimed at finding out, whether I am wrong in seeing inflation here in this proposal of a temporary, if you please, increase. We are always told in the beginning that inflation will be temporary, but usually they develop into calamities of much longer duration, and I am trying to find out whether there is or is not here a temporary inflation of purchasing power backed by the creation of an artificial purchasing power.

Mr. **Brougham**. By the application of this bill, you mean?

Mr. **Luce**. Yes.

Mr. **Brougham**. No; there is no inflation for the reasons that I have stated. It is seen to, first, that the rate of production shall rise concurrently with the rate in the increase of money, and so long as that is fulfilled, the price level cannot rise.

Now, I am a stabilizationist. I am against the reflationist idea of Irving Fisher. I do not believe in it. I think that we can get along comfortably on whatever price level we happen to be on, and stabilize that, and this bill fulfills the condition of that.

Mr. **Spence**. May I ask you a question? Maybe the answer is obvious, but I do not know it.

This bill merely proposes to operate upon the retailer and the consumer. It gives the retailer a higher price, that the consumer pays, but the slack is taken up by society, for the general benefit of society.

Mr. **Brougham**. That is just the point at which the new credits are applied.

Mr. **Goldsborough**. It does not give the retailer a higher price.

Mr. **Spence**. It gives the retailer the going price?

Mr. **Brougham**. Yes, sir.

Mr. **Goldsborough**. If the retailer should jack up the price, he would lose his license.

Mr. **Brougham**. And also the corner grocer, across the way——

Mr. **Spence**. It does not operate upon anybody but the retailer?

Mr. **Brougham**. Oh, yes; upon all factors of industry.

Mr. **Spence**. It gives the consumer an additional purchasing power, but what is to prevent the producer, the wholesaler, the manufacturer, or the distributor from jacking up his price in order to absorb this 15 percent that we are attempting to give to the purchaser? Would it not be natural for him to do it? Isn't the price on not only the raw material but on everything down to the finished product to the consumer based upon the price that the ultimate consumer should pay, and wouldn't they naturally raise their prices in order to obtain this benefit, rather than to have the purchaser obtain that?

Mr. Brougham. That touches the point that I adverted to when I began and suggested an amendment, that would prevent that.

Mr. Spence. In the bill now, is there anything that would prevent that?

Mr. Brougham. I think that there is not in the bill, and I think it is defective to that extent, but it is possible for your committee to put in the amendment, which would fill that gap.

Mr. Transue. One question. The interbank currency is backed by the credit of the United States, is it not?

Mr. Brougham. It is backed by the goods of the United States.

Mr. Transue. By the credit of the United States; that is, the United States Government is behind that interbank currency that you are giving to the bank and that they will accept. Otherwise they would not accept it.

Mr. Brougham. Oh, certainly.

Mr. Transue. Then, of course, that is just another way of using the credit of the United States, and, if it is paid at all, it will have to be paid by the taxpayers of the country.

Mr. Brougham. Not by the taxpayers of the country in money, but by the people of the country in goods and services which they are now not producing and are anxious to produce.

Mr. Ford. Right at that point, let met make an observation. If you can convince, or anybody can convince the country and the Congress that this interbank currency will not be a Treasury liability, but will be repaid in excess production and in consumption to meet that production, I think it will solve the problem. That is the crux of the whole matter, as to who is going to pay the bill that the interbank currency will create in the end.

Mr. Brougham. Before that currency is put out, there has been a transaction and goods have been sold at an increased rate, a 20 percent increased rate. They have already been sold, and they have paid for that currency in advance.

Mr. Ford. I appreciate what your philosophy is——

Mr. Brougham (continuing). Then that currency goes on in circulation and is paid for in cash in each transaction with goods and services that were not effectuated before.

Mr. Ford. That is exactly what you are going to have to prove to the country and to Congress, that that is the situation. I am inclined to agree that, if that were possible, you may have the solution to the present problem.

Mr. Crawford. Referring to the question that we were discussing a while ago with reference to reserve requirements, do you consider at the present time that the Board of Governors of the Federal Reserve Board regulates the supply of money or the loanable funds that we have?

Mr. Brougham. No; it does not. It does to a certain extent.

Mr. Crawford. Let me ask you in another way this question: Do you consider that that is one of the purposes for their being in existence?

Mr. Brougham. One of their purposes is to regulate the flow of money in the United States for the accommodation of trade and manufactures.

Mr. **Crawford.** Do you also consider that it is empowered to regulate the aggregate flow of moneys?

Mr. **Brougham.** Yes; by various methods, like the regulation of the discount system, and the regulation of reserves.

Mr. **Crawford.** Do you mean to say that you feel that the regulation of the flow of money is the same as the regulation of the amount of loanable funds, one and the same thing?

Mr. **Brougham.** One and the same thing; yes, sir.

Mr. **Crawford.** I do not quite see it that way, but I wanted to get your advice on it. I have felt that the Board was more or less empowered to regulate the supply of loanable funds, and in view of the statement made here before the committee one day in answer to an interrogration I put to Governor Eccles, I have not understood that the Board was authorized or empowered or that it was supposed to be authorized and empowered to regulate the flow of money.

Now, it seems to me that if they are empowered to regulate the flow of money, they are to the same extent empowered to synchronize the flow of money with the flow of goods.

Mr. **Brougham.** They are not empowered that much. By regulating the reserves, they have cut down the base on which money can be issued as loans to a certain extent. They cannot do it any further. Conceivably they might need to do so, or conceivably they might need to reduce the reserves required now, and to that extend that would have an effect upon the flow of money.

Mr. **Crawford.** Then would you say that in order to empower them to regulate the flow of money so that it can be synchronized with the flow of goods, as we have under discussion in this bill, it would be very necessary to give them the additional powers which they do not have now?

Mr. **Brougham.** If they had perfect power to regulate the flow of money, they should have the power to issue the money exclusively, according to the terms of the first article of the Constitution. Instead of that, there are 15,000 mints throughout the country, that are minting credits irrespective and according to the views of their localities and according to the psychology of the bankers and of borrowers, and the Federal Reserve Board has no control over that.

Mr. **Crawford.** That was my understanding.

Do you think that empowering the Federal Reserve Board to make grants to the Treasury and thereby control the flow of money would enable the Board to synchronize the flow of money with the flow of goods?

Mr. **Brougham.** That proposition was made before this committee the other day by Mr. Cromwell, and to a certain extent it can be done in that way, because it would result naturally in a remission of taxation which would be felt throughout the country as an increase of purchasing power to the extent that it was done. My only fear is that that use of new money created by the Government would not be sufficient. I should prefer a more immediate and a more widespread distribution of new money by the Government as proposed in this bill as a universal discount on prices at retail.

Mr. **Crawford.** Do you think this method would be simpler and therefore more effective than that of making grants through the Board?

Mr. **Brougham**. It would be quite as simple, and it would be far more effective.

Now, some point has been raised about the administration of this bill. When you and I stop at a gasoline station we find automatically registered the State and the Federal taxes when we pay for 3 gallons of gasoline. There is no difficulty in the machinery. The National Cash Register Co. could send a representative here before your committee and could explain to you how this reversed sales tax could be remitted to the American people automatically with every transaction, and every transaction recorded.

Mr. **Crawford**. That is all that I have to ask.

Mr. **Goldsborough**. The committee will adjourn until half past 10 tomorrow morning.

(Thereupon, at 12:26 p. m., an adjournment was taken until Thursday morning, February 17, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, FEBRUARY 17, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The hearings on H. R. 7188 were resumed at 10:55 a. m., Hon. T. Alan Goldsborough presiding.

Other members of the committee present: Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Evans, Mr. Transue, Mr. Gifford, Mr. Luce, and Mr. Crawford.

Mr. Goldsborough. The committee will come to order, please.

Prefessor Weyforth, will you come forward, please?

STATEMENT OF WILLIAM O. WEYFORTH, ASSOCIATE PROFESSOR OF POLITICAL ECONOMY, THE JOHNS HOPKINS UNIVERSITY

Mr. Goldsborough. Will you state your full name for the benefit of the record, please?

Mr. Weyforth. William O. Weyforth.

Mr. Goldsborough. Will you state your connections, please, sir?

Mr. Weyforth. I am associate professor of political economy at the Johns Hopkins University.

Mr. Goldsborough. Now, Professor Weyforth, we are considering H. R. 7188, as you know. Do you prefer to complete your statement before you are questioned, or otherwise?

Mr. Weyforth. Well, the statement is very brief. Perhaps it might be just as it suits you.

Mr. Goldsborough. How long will it take?

Mr. Weyforth. I do not think it will take more than 10 minutes.

Mr. Goldsborough. Proceed. We will defer questions until after you have completed your statement.

Mr. Weyforth. One of the outstanding economic problems confronting the people of the United States at the present time is the management of the currency of the country. Whether or not one believes in an international gold standard along pre-war lines, under which the credit policy of the banking system was subject to more or less automatic determination according to the state of the gold reserves, the fact remains that at the present time such a credit policy is impracticable. If bank credit were expanded to the full extent that might be possible on the basis of the present huge gold reserves of the country, an unconscionable inflation would doubtless be fostered. Under these circumstances new guides for credit policy must be found and willy nilly we find ourselves with a managed currency.

Probably every one would agree that, if we must have a managed currency, for the time being at any rate, it is desirable that it should be managed in such a way as to contribute, so far as currency management can do so, to the full utilization of the productive capacity of the country; and when production has thus been raised to this high level to stabilize it there.

It is one thing to envisage a broad purpose such as this, but it is another thing to determine the specific policies that will achieve the end desired. Unfortunately no generally accepted clear-cut guides are available for the credit authorities.

This bill, however, endeavors to make a contribution to the solution of the problem by setting up a formula, which would be an important factor affecting the volume of bank credit.

The plan embodied in this bill, as I understand it, is based upon the assumption that when there is, at any time, large unused productive capacity, this is due to the fact that there is not sufficient purchasing power available to take off of the market the full potential product of industry at prices that will cover the cost of production.

Presumably the full potential product of industry might be disposed of if there were sufficient reduction of prices. But if these reduced prices did not cover costs, under a regime of private enterprise, the incentive to carry on productive operations would not be present and there would be relative stagnation.

It is apparently the purpose of this bill to overcome such a difficulty, by compensating retailers for making such reductions in prices as may be necessary to sell the full potential product of industry. For this purpose retailers are to be provided with bank deposits equal to the amount of their price reductions; and the banks in turn are to be compensated through the issuance to them by the Government of an equal amount of so-called interbank currency notes, which may be counted as reserves and used in the settlement of interbank balances but may not be paid out into general circulation.

The amount of price reduction for which compensation to retailers is to be allowed is to be determined by a Federal Credit Commission. The basis for the Commission's computation is to be a statistical calculation of the full productive capacity of industry as compared with unused productive capacity. The possibility of making any such calculation for industry as a whole is doubtful. But let us assume for the moment that such a calculation is made and it is found that while the full capacity is represented by, let us say, 100, the capacity actually in use is represented by 80 and there is consequently unused capacity of 20 percent.

It is assumed, then, that the price reduction for which compensation should be allowed is 20 percent, and that this same reduction should apply to any retail commodity or service whatsoever without any variation.

Mr. **Goldsborough**. I do not know whether you noticed it, but the bill provides for 15 percent.

Mr. **Weyforth**. That is the original, until they made this calculation?

Mr. **Goldsborough.** No, sir. There will always be a 15 percent cut between consumption and production, so there will only be a raise there of 5 percent.

Mr. **Weyforth.** My understanding in reading the bill was that the 15 percent applied originally, before the Commission was able to make its calculation, and that after the Commission had made its calculation, the reduction that would apply would depend upon the amount of unused plant capacity.

Mr. **Goldsborough.** You are entirely correct about that, Doctor. As one attempt to avoid inflation, the bill states that there should be no effort to fill the gap between production and consumption.

Mr. **Weyforth.** Yes; but suppose that the unused plant capacity is 20 percent; then do I understand that the reduction in price is to be 20 or 5 percent?

Mr. **Goldsborough.** Only 5 percent.

Mr. **Weyforth.** I think the principle of what I have to say would apply, although the figures would have to be changed.

Now, it seems to me that right here a fundamental economic misconception is involved. The plan assumes that if the amount of any goods that will be purchased at a certain price is 20 percent less than the amount that is offered at that price, a reduction in price of 20 percent will cause exactly the full amount previously offered to be purchased.

Is that clear? It is assumed that if you have a certain amount offered for sale, and it cannot be sold at the existing price, and the amount that would not be sold at the existing price is 20 percent of the total amount, then by cutting prices by 20 percent you could sell the whole amount.

Mr. **Williams.** That would not necessarily follow.

Mr. **Weyforth.** No; I do not think it would.

Mr. **Goldsborough.** You see the buying public could use that discount wherever they saw fit. It would go through the economic system at retail.

Mr. **Weyforth.** Yes.

Mr. **Patman.** You would not pick out certain commodities, would you?

Mr. **Weyforth.** I understand that this bill is to apply to all commodities.

Mr. **Patman.** If the people in making their purchases should select certain commodities, there would soon be a shortage of those particular commodities and a surplus of the others.

Mr. **Weyforth.** That is the point I want to make.

Mr. **Patman.** I beg your pardon.

Mr. **Weyforth.** I want to point out that, as a matter of fact, there is no such mechanical relation between the prices of any goods and the amount purchased. In the cases of some goods a small reduction in price will lead to a considerable increase in the amount purchased, whereas in other cases it is very difficult to stimulate increased buying even with quite decided reductions in prices. This is the distinction that economists make between elastic and inelastic demand. There is no uniformity among the thousands of commodities and services offered for sale.

Consequently a uniform compensated price reduction of 20 percent under the circumstances just mentioned might in some industries stimulate buying far boyond their present productive capacities, while in other industries it might still be insufficient to bring about equilibrium. These difficulties would be enhanced by the fact that the uniform price reductions provided for are to be based upon the average unused productive capacity in all industries. But such an average may conceal vast differences in individual industries. At the very time when one industry has unused capacity of 50 percent another industry may be operating at nearly full capacity. But if the average unused capacity in all industries is estimated at 20 percent, is there any reason for believing that a 20-percent reduction in the prices of the products of each of the above industries will bring about just a full utilization of the capacity of each industry?

Mr. **Gifford**. Right there, the prices of salt and pepper should be as persuasive as those on wheat and cotton.

Mr. **Weyforth**. On salt and pepper, the demand is inelastic. The people buy the same amount whether the price is low or high.

Mr. **Gifford**. I do not mean literally salt and pepper, but I mean small quantities of things. Take the average price; it may have gone up or down but little, and to weigh them in with wheat or cotton and strike an average is not quite the best way to get an index, is it?

Mr. **Weyforth**. I think not.

Mr. **Gifford**. That is the argument that has been used a good deal on the stabilized dollar, that it is based upon index prices. Do you agree with that?

Mr. **Weyforth**. I do not think that you can use a general average for this purpose here.

Mr. **Gifford**. Are you familiar with the way they do find the index?

Mr. **Weyforth**. In a general way.

Mr. **Gifford**. Isn't the method they use the adding together of the prices of thousands of commodities? That has never been cleared. though I asked that question many times. The commodity-dollar argument has referred to the usual way, and this bill refers to the usual method of finding the commodity index.

Mr. **Weyforth**. There are various ways of making index numbers. Sometimes it is an unweighted average, and sometimes it is a weighted average.

Mr. **Williams**. What does the Bureau of Statistics in the Department of Labor use?

Mr. **Weyforth**. I think theirs is a weighted average.

Mr. **Williams**. That is the one that is generally referred to.

Mr. **Weyforth**. Generally used; yes.

Mr. **Gifford**. What I wanted to ask is, did you ever see one of those made up that was satisfactory to you, that was dependable?

Mr. **Weyforth**. They are useful for certain purposes. I think the general feeling among economists nowadays is that you cannot use one index number for a great many different purposes. Originally the idea was that if you got an average of a large enough number of prices, you could use the index number to serve a great many different purposes, but the feeling now is that you cannot do that.

Mr. **Gifford**. Do you think it can be done satisfactorily, based on the commodity dollar, so called?

Mr. **Weyforth.** You mean to provide a basis for a commodity dollar?

Mr. **Gifford.** Yes; or any other name that you want to call it.

Mr. **Weyforth.** I do not believe that we can base our monetary policy upon any single index like that. I think the problem is far more complicated than that.

Mr. **Gifford.** You have never seen an index that would probably be satisfactory to you?

Mr. **Weyforth.** I have not.

If to these objections it is replied that the compensated price reduction for each commodity or service might be adjusted so as to meet the requirements of each individual case, then I am afraid that the answer must be that this is an undertaking beyond the competence of any administrative body.

Mr. **Goldsborough.** Might I interject at that point that I would personally never support a bill of that kind.

Mr. **Weyforth.** Yes.

Thus there is no reason to believe that the measures proposed in the bill offer any possibility of achieving that full operation of productive capacity which it is the purpose of the plan to promote.

On the other hand, if this is merely a plan to increase the quantity of money in circulation, which in some way is to be controlled by the Secretary of the Treasury and the Federal Reserve Board so as to prevent inflation, there seems to be little point in undertaking the elaborate statistical calculations provided for in the proposal.

The bill seems to me to be loosely drawn. Its language is at times obscure. It provides no intelligible criteria for the retirement of the currency which might be issued under its terms, and it would probably present administrative problems of almost insuperable magnitude.

I have not commented upon these other matters in my testimony since, aside from such objections, however important they may be, the plan, I think, would be unworkable because based upon a fundamental misconception of the operation of the price mechanism as I have just endeavored to point out.

Mr. **Goldsborough.** Mr. Reilly, have you any questions?

Mr. **Reilly.** No.

Mr. **Ford.** I would like to ask a question.

What you are trying to point out is this, that with a 20 percent reduction in price, assuming that there was a 20 percent increased production of goods, they would be of such a diverse character that some of them would be over-produced—for instance, there would be an outmoded gadget that the people are no longer using, and other goods would be overproduced because of the miscalculation that the manufacturer made of the market, and in those two cases the volume of money in the hands of the purchasers would not mean a thing. Then there is a type of goods that everybody wants. We will assume that only 80 percent of the people have purchasing power, are capable of buying. So there is a 20 percent lag there, and if some mechanism were provided to put that buying power in their hands, it would probably take up the shortage, and I was just about to comment this morning that possibly the question of price would not necessarily balance the volume; there must be some other mechanism, an even more complicated mechanism, devised that would distinguish as between commodities in order that the mechanism proposed here would be operative.

Isn't that probably what you meant?

Mr. **Weyforth**. That was in my mind; yes. It would have to be a much more complicated procedure.

Mr. **Ford**. I have been giving this bill a lot of thought, knowing as I do the deep sincerity of the author of it, Mr. Goldsborough, and that he had in mind just one thing, and that is to accomplish what we all conceive to be desirable and almost vital, but I have, after thinking about it, about decided that perhaps the mechanism proposed is not good, and I was thinking of another angle, and this is just a suggestion, that possibly, in attempting to take off this surplus, we might have tackled it at the wrong end, and I am wondering if some device might not be worked out, possibly, whereby we could attack it at the production end, where a manufacturer was producing a very desirable article and a much needed article, an article that would be purchased when money is available, and I was wondering if some mechanism might not be devised whereby we could compensate him in the regular way in producing those goods at a price at which people could purchase them.

Would you say that there was a possibility of changing the base of application in that way?

Mr. **Weyforth**. I am afraid the difficulty would be that we would be compensating producers for producing things that people did not want. Take one of these commodities, for example, that has gone out of fashion——

Mr. **Ford**. There are two things that would enter into it that might block up this program. One is a commodity that the people no longer wanted, and the other the commodities that, though the people were able to buy them, they would not buy.

Are not those factors in this problem?

Mr. **Weyforth**. If you compensate producers for producing more goods than would be purchased by the community, I do not know where you are going to stop that procedure.

Mr. **Ford**. I can conceive of this, that when we have more goods than can be purchased—and, you know, Ben Butler said a long time ago that it was not oversupply, but underconsumption, that was the trouble, and what he meant by that was the ability of consumers to purchase. There are just millions of things on the market that millions of people would purchase if they had the ability to do so.

Mr. **Weyforth**. But it is a question of having the proper adjustment of production. It may be that too much of one thing is being produced and too little of another thing is being produced, and if you continued compensating producers for producing the thing that people do not want, you keep productive capacity from going into other industries and producing things that people really want.

Mr. **Ford**. I would say that this would be one of the primary objectives of this bill. I would say that there are a lot of things that people would buy, and others that they would buy in greater quantity, if they had the purchasing power to do it with. We all know that. But on the other hand there are commodities being produced that there is no longer a demand for, or that only an odd person wants. There are other commodities being produced in excess of the market, where the people have got all that they want of them, and I should say that those two elements would enter into this particular scheme. But to say that just a flat reduction of price as against an overproduction of quantity would cure it—well, it may be that my thinking is crooked, but it has led me to the conclusion that that probably is not the solution.

Mr. Patman. I want to ask you some questions on the bill, sir.

I understand that the purchases at retail aggregate each year about 40 billion dollars. Is that your understanding, Doctor?

Mr. Weyforth. I really do not know.

Mr. Patman. Mr. Goldsborough obtained the figures from the Department of Commerce, and I presume that they are correct.

I wonder what part of those purchases would be made by corporations? Would you have any idea?

Mr. Weyforth. No.

Mr. Patman. Would you, Mr. Goldsborough?

Mr. Goldsborough. No.

Mr. Patman. I mean the percentage. Well, let us say that 25 percent of the purchases were made by corporations. I presume that that would be conservative, in view of the fact that the corporations control a large part of this country?

Mr. Weyforth. Retail purchases?

Mr. Patman. Yes; retail purchases.

Mr. Weyforth. Twenty-five percent made by corporations? I do not know.

Mr. Patman. Well, we will say from 10 percent to 25 percent. I suspect that that would be reasonable.

Now, let us say that you are one of the directors of a corporation, and under this bill corporations cannot obtain the benefit of the discount, but individuals can. I just wonder if it would be possible to administer the law, in view of the fact that an officer of a corporation could individually go out and buy anything that the corporation wanted and obtain a 15 percent discount. There are no strings on their selling it to anybody they wanted to, as an individual.

Then let us suppose that you turned around and sold that to the corporation, and gave it the benefit of the 15 percent discount, if you wanted to, because the corporation would have to pay the full price if it went into the open market, but you could sell it to the corporation at 15 percent less, or you could obtain a profit of whatever you felt your services were worth.

Now, do you believe that it would be impossible to administer that law, when we say that this discount is obtainable by individuals and persons, but not obtainable by corporations?

Mr. Weyforth. I think the administrative difficulties would be tremendous.

Mr. Patman. Do you think it would be possible to administer it?

Mr. Weyforth. I do not see how it would be.

Mr. Patman. Another question. There are approximately 1,500,000 retail outlets in this Nation. That includes everything from peanuts to automobiles, all kinds of retail outlets. Under this bill, of course, all of these retail outlets would have to obtain a license, and that would cost considerable to administer, as far as that is concerned, I presume.

Now, do you think that it would be right to freeze in the hands of a few people the right to distribute goods and grant a 15 percent discount? Do you not think that that is a privilege anybody should be permitted to enjoy, if they place themselves in a position to distribute goods?

Mr. **Weyforth.** I assume that anybody could get this license.

Mr. **Patman.** I suspect that that assumption is correct. That being true, then, this retailer really has a right to obtain a credit on Uncle Sam, which is the same for all practical purposes as carrying the signed checkbook of Uncle Sam. All that he has to do is to fill in the amount. Mr. Goldsborough testified in connection with this bill that nothing will be required of the consumer at all; that he won't have to sign anything; but that the man who is running the store goes to the bank and he signs up whatever is necessary to get that credit, and so for all practical purposes he has Uncle Sam's check already signed, and all that he has to do is to fill in the amount. He can say that he sold John Doe an automobile for $1,000 and that he wants $150, and all he will have to do is to fill that in.

That is the way you understand the bill?

Mr. **Weyforth.** That is right.

Mr. **Patman.** I asked one of the witnesses before this committee about farmers. Many of them sell their hay to their neighbors, and they sell to people in adjoining communities, and they sell eggs and butter and different things, but these farmers would not be privileged to get that discount. Therefore, if I were ordinarily buying from the farmer, I would say to him, "I cannot pay you this price, because you cannot give me the discount. I will have to buy from the store." This man that I am referring to was a social-credit man; he was the man who is a great believer in this Engineer Douglas' theory, and he wrote me that under this bill it is contemplated that everybody would be licensed, and if this farmer wanted a license it would be perfectly all right for him to get a license.

Do you think that our Government would be stable very long if we indiscriminately gave everybody an opportunity to draw on Uncle Sam every amount that he wanted to?

Mr. **Weyforth.** I do not see how it can be worked out. Of course, another problem would be what would be the price from which this reduction would be calculated.

Mr. **Patman.** In other words, they could increase the price from $1 to $1.15 and not have any reduction at all?

Mr. **Weyforth.** That is right.

Mr. **Patman.** There is no control over that?

Mr. **Weyforth.** There is no control over it.

Mr. **Patman.** On account of the interest of Mr. Goldsborough in this bill, and on account of his enthusiasm for it, I have given it very careful consideration, but I just cannot see how the administrative provisions can possibly be worked out; I just cannot see it—and you agree with that?

Mr. **Weyforth.** As I stated, I think that the administrative problem is insuperable.

Mr. **Patman.** In fact, do you not think that it is impossible?

Mr. **Weyforth.** Insuperable, I should say.

Mr. **Meeks.** May I ask a question? I have not asked anybody a question yet, though I have thought a good deal about it.

Did I understand that the general purpose of this bill is to establish an equilibrium between production and consumption? That is the objective of it, is it not?

Mr. Weyforth. That is right.

Mr. Meeks. So that it reaches very deeply into the general affairs of all of our people?

Mr. Weyforth. That is correct.

Mr. Meeks. And vitally affects the lives of the people. Now, do you think, or have you given any thought to this question, that there is any possibility by any general legislation to accomplish that end?

Mr. Weyforth. I do not know of any.

Mr. Meeks. We have gone into the details of this bill a great deal, but we have not gone into the general subject—at least I have not heard of anybody doing so—of its application to any legislation that can be devised to reach the objective of this bill?

Mr. Weyforth. I do not know of any.

Mr. Meeks. I was interested in your reaction to that.

Mr. Weyforth. Yes.

Mr. Meeks. You do not think it can be done?

Mr. Weyforth. I do not know of any way. It may be able to be done, but I do not know how it can be done.

Mr. Meeks. It has not been done yet?

Mr. Weyforth. It has not been done yet; no, sir.

Mr. Patman. Let me pursue that question, if you are through.

Mr. Meeks. Yes.

Mr. Patman. Suppose this farmer gets his license so as to grant a discount on eggs and butter, there is nothing to keep him from selling peanuts, is there? If he gets a license to sell butter, he can sell automobiles, or steam engines, or clothing, or hardware?

Mr. Weyforth. I should assume so, unless the regulations would specify what articles he was permitted to sell.

Mr, Patman. There is nothing in the bill that requires him to confine his business?

Mr. Weyforth. No.

Mr. Patman. In other words, he could sell everything from peanuts to automobiles.

Mr. Ford. He could not sell automobiles, because he would have to have a franchise from the automobile manufacturers.

Mr. Patman. Suppose that he bought them from the automobile dealer, and got the 15-percent discount from him, and then sold them?

Mr. Meeks. Or sold used cars.

Mr. Patman. Yes; and then sold them.

Mr. Spence. What are the elements that enter into the price of goods, Professor?

Mr. Weyforth. Well, the economists usually say supply and demand.

Mr. Spence. Demand largely makes the price. Isn't that true?

Mr. Weyforth. Well, demand in conjunction with the supply.

Mr. Spence. But the converse is, according to your theory—and I think it is sound—that while the demand makes the price, the price cannot make the demand?

Mr. **Weyforth.** It affects it, of course, and to different degrees with different commodities. A 10-percent reduction in price in the case of one commodity might mean a very great increase in the amount purchased, and a 10-percent decrease in another would not make any difference.

Mr. **Spence.** It would not persuade men who did not want the article to buy it? It is all based upon demand?

Mr. **Weyforth.** Yes.

Mr. **Spence.** People won't buy the things they do not want, even though they can get a very much reduced price.

Mr. **Weyforth.** Unless the thing is absolutely useless, they might be induced to buy things if you cut the price low enough. In the case of automobiles, they can make about 5,000,000 a year, but people do not buy them at present prices. If the prices were cut in half, they might be able to sell them.

Mr. **Spence.** People would buy automobiles at any price.

Mr. **Ford.** No; the minute that they raised their prices this year, sales stopped, when they raised the price on an average car about $115, so price does have some relation to demand.

Mr. **Weyforth.** It has a very important relation. I think that you could sell almost any reasonable amount of any commodity if you cut the price enough.

Mr. **Williams.** There would be a large number of people, or at least a substantial percentage of them, who would not have the need for this discount and therefore would not purchase more than they are purchasing right now, would there not?

Mr. **Weyforth.** That is true.

Mr. **Williams**, What percentage of the people would you say are in that class?

Mr. **Weyforth.** It would be impossible for me to say.

Mr. **Williams.** Would you say it is as much as 25 percent?

Mr. **Weyforth.** You could not say. It would vary, of course, with different commodities.

Mr. **Williams.** Do you know the percentage of the people in this country who have an income of $2,500 a year; that is, a family income of that?

Mr. **Weyforth.** I have heard it, but I do not remember just now.

Mr. **Williams.** I think it is estimated to be from 20 to 25 percent.

Mr. **Weyforth.** I did not realize it was that much.

Mr. **Patman.** About seven and a half million families, I understand.

Mr. **Williams.** I think it has been estimated by the Brookings Institution to be from 25 to 30 percent.

Mr. **Weyforth.** All right.

Mr. **Williams.** This bill would be furnishing that discount to that class of people, who really do not need it and ought not to have it, as a matter of fact?

Mr. **Weyforth.** I do not see how you could distinguish between different groups of people.

Mr. **Williams.** I do not think that you can; but that is one of the defects in this bill, that the Government will be financing, or rendering aid and assistance, or relief, to a class of people that under our economic set-up and under their financial condition do not need it and would not use it if they had the opportunity. In other words, what benefits they received from it would go into their savings accounts rather than into the consumption of goods. Isn't that true?

Mr. **Weyforth**. That is possible.

Mr. **Williams**. Now, what I am interested in, and you have given this bill study, is the provision which provides for the withdrawal, in case of necessity, of this interbank currency.

Mr. **Weyforth**. That was obscure to me. I did not understand how that would work.

Mr. **Williams**. Do you understand, to start with, that it is put into the banks to make up the deficit caused by giving credit to the retailers?

Mr. **Weyforth**. That is right.

Mr. **Williams**. In other words, on the basis of 15 percent, the retailer comes into the bank and deposits $850 and receives credit on the books of the bank for $1,000. That is an absolute deficit so far as the bank account is concerned, of $150, is it not?

Mr. **Weyforth**. The bank gets that from the Government in the form of interbank currency.

Mr. **Williams**. This interbank currency comes in to make up that deficiency?

Mr. **Weyforth**. That is right.

Mr. **Williams**. When the time comes for the Government to withdraw that $150 of interbank currency that it put in there, what takes its place?

Mr. **Weyforth**. I was wondering about that very thing myself. I do not know. If you can decrease the assets of the banks without any reduction in their liabilities or without any new assets to take the place of the thing that was taken away from it——

Mr. **Williams**. That has been my contention all the time, that it would be creating a bankrupt condition of the banks.

Mr. **Weyforth**. It would take some asset from the bank, and you would have to have either a reduction in liabilities or another asset to take its place.

Mr. **Williams**. There has been some talk as to whether it is an asset. It is an asset of the bank, is it not?

Mr. **Weyforth**. If not, the bank would never get its books balanced.

Mr. **Williams**. When you take it out the books are unbalanced? There is not any other conclusion to that?

Mr. **Weyforth**. I do not see any.

Mr. **Crawford**. Let me ask you this question, which is based on our practice heretofore: In our farm bill just passed there is a proviso which directs loans to be made by the Commodity Credit Corporation, and the bill specifies, in substance, that on certain commodities those loans shall be made at a rate of not less than 52 percent and not more than 75 percent of parity. Now, suppose that the parity price of cotton is 16 cents, say, or 17 cents a pound at the present time, and that the market is 8 cents a pound, and the loan can be made by the Commodity Credit Corporation considerably in excess of the market under the provisions of the agricultural bill.

Does that not bring into the price element now a factor which sets the price on the commodity instead of demand setting the price, as you stated awhile ago?

Mr. **Weyforth**. I should think it would. Doubtless the holder of cotton would not sell it for less than the amount that he could borrow on it, so that the price could not go below that amount, I should imagine.

Mr. **Crawford**. In other words, would you say that we have now entered an era where demand does not make the market price but that the market price is established by artificial factors injected into the picture which have no relation to the demand?

Mr. **Weyforth**. Unless you look upon an artificial demand as an element of demand itself. It is not demand in the sense that it is usually understood.

Mr. **Crawford**. In other words, it is not consumer demand or market demand, but a demand created by the credit of the Government being used to push the price up above what the world is willing to pay?

Mr. **Weyforth**. I should think so.

Mr. **Crawford**. Do you know of any way, operating along the lines of this bill, whereby purchasing power can be given to the consumer or placed in the hands of the consumer without the price element being burdened with the carrying costs of that purchasing power so provided to the consumer?

If my question is not clear——

Mr. **Weyforth**. I am not sure that I understand what you mean.

Mr. **Crawford**. If you are running a factory, and you borrow money to finance inventories or capital structure, the interest on those borrowings works into and comes out as an element of the cost of the finished product, does it not?

Mr. **Weyforth**. That is right.

Mr. **Crawford**. Therefore, the price which you make to the consumer must involve all of the distributions which you have made and any actual cash, such as wages and salaries, and it involves your overhead cost and interest charges?

Mr. **Weyforth**. Right.

Mr. **Crawford**. It seems to me that this bill, if operated, would somewhat get around that, in that the price charged to the consumer would not necessarily cover all of those cost elements.

Mr. **Weyforth**. That is right.

Mr. **Crawford**. Prior to that.

Now, do you know of any way in our present system of credits, currency, banking, and money, or out of our present system, whereby the objectives can be obtained so that the goods can be sold to the consumer at a lower price without wrecking your capital structure?

Mr. **Weyforth**. I do not know how it can be done. Of course, I think that the increase in purchasing power comes primarily from business spending. Business spending, I think, is developed after we have a depression by the fact that costs have been reduced. I do not know how much they have been during this depression, but costs as a rule, after a period of depression, have been reduced, wages usually have come down, interest charges usually have been reduced either because the rate of interest has been decreased or bad debts have been wiped out. That puts the producer in a better position to meet his cost, because his cost has been reduced. Then a revival of demand is likely to come because goods have worn out during the period of deficient consumption, machinery has worn out and become obsolete, inventories have been reduced, new industries developed. You have the stage set then for an increase in business spending, and with your increase in business spending, more people are employed. They are provided with additional wages and consumers have more purchasing power. It seems to me that that is ordinarily the way in which revival comes about.

Mr. **Gifford**. Supplementing that, you noted the startling advice recently given to business men, to go out and get orders and lower prices to get volume; that is, if you are losing money, lose more.

Mr. **Weyforth**. Lose on each unit, but make it up by selling more units?

Mr. **Gifford**. Get volume.

Mr. **Weyforth**. I think it may be desirable, in the interest of business at times, to cut their prices rather than try to maintain them, in order to cause the flow of goods to occur. But that is a question.

Mr. **Gifford**. There are some goods that must be gotten rid of at times.

Mr. **Weyforth**. Yes.

Mr. **Crawford**. You say, cut the price in order to increase the flow of goods. You mean that if you cut the price, by doing so you can increase the flow of goods which can be moved at the cut price above the cost of production with the increased flow?

Mr. **Weyforth**. Exactly, yes.

Mr. **Crawford**. But, that element being missing, you would not advocate cutting the price?

Mr. **Weyforth**. Well, there may be times when it would be desirable even then. It is true of a great many business concerns, that they do sell their goods at a price lower than the cost of production. They want to keep their plants going, and they find it more desirable to do that than to shut down.

Mr. **Crawford**. As a temporary expedient.

Mr. **Weyforth**. They cannot do that permanently, of course.

Mr. **Crawford**. Let me ask you this question, which I think fits into the situation at the present time. If you will go through the country today, and check the warehouses, you will find that many producers have heavy stocks of goods on hand. Do you feel that the conditions at this moment are such that the holders of those goods should reduce their prices, and, having in mind that they are not going to cut wages or salaries, start moving those commodities into the consuming market on the reduced price, anticipating that later on they will pick up a volume which will accommodate their situation to the losses that they take on the present inventory?

Mr. **Weyforth**. That may be expecting too much of them. Of course, we do know that they actually do cut prices, and they have been going down in the last few months. They were not anxious to do it, but evidently they saw the need of moving their stocks of goods and felt it more desirable to dispose of them even at lower prices rather than continue holding them.

Mr. **Crawford**. They can properly do that until the margin of profit is eliminated.

Mr. **Weyforth**. Eventually, if they cannot cover their costs, they will go bankrupt.

Mr. **Crawford**. Just as sure as they continue that policy?

Mr. Weyforth. Certainly.

Mr. Crawford. The reason that I was interested in getting your reaction on it is that I am officially informed by the officers of a number of institutions that they intend to sit tight and liquidate their inventories without cutting the price by keeping the plants closed unil those inventories are reduced.

It seems to me that our training and education under N. R. A. brought the manufacturers of this country quite a bit into line with the philosophy which says, "Stick together; hold your prices, and let production go by the wayside."

Mr. Weyforth. I think that that may be one of our difficulties. That gives you that rigidity in the price system which seems to me to prevent the readjustments from occurring which are necessary to keep the economic system moving. That is one of our troubles. So many of our prices have become rigid, prices of commodities, prices of labor. They do not move and adjust themselves to new conditions, and the result is that we have stagnation.

Mr. Goldsborough. They are not regulated by the law of supply and demand, then.

Mr. Weyforth. They are.

Mr. Goldsborough. You just said that they were rigid.

Mr. Weyforth. But it is the control over supply that makes them rigid.

Mr. Crawford. Would you go so far as to say that you feel that the agricultural bill just enacted would tend to put rigidity in the prices of foodstuffs?

Mr. Weyforth. I would rather not answer that question, because I am not familiar with the provisions of the agricultural bill.

Mr. Crawford. Would you go so far as to say that this rigidity you speak about tends to block production and eliminates the freedom of the market, or free flowing of goods?

Mr. Weyforth. I think there is a tendency in that direction; yes, sir.

Mr. Crawford. Would you say that there was a little bit more than a tendency?

Mr. Weyforth. Well, perhaps more; yes.

Mr. Gifford. There is a little thought there on supply and demand that I wanted to interject. You take the basement of a large department store; they create a demand by advertising lower prices if you go downstairs, but if a lady sees a bonnet upstairs that is a little different, has little different feather on it, she will pay 10 times as much for it. Co the business men have been shrewd enough to resort to all sorts of schemes to get them to buy, without much reference to the item of cost. Demand is not always based on cost, is it?

Mr. Weyforth. It is a question of demand. The ladies demand those things, and they are ready to pay for them.

Mr. Gifford. Did your wife ever pay more for a bonnet than you thought she should?

Mr. Weyforth. I do not have a wife. I am a bachelor, so that I am not familiar with those things.

Mr. Goldsborough. You have discussed at some length this bill, and you evidently, as far as I can see—and I may be mistaken—base your conception of its results on the usual conception of the law of supply and demand.

Now, when the harvester trust sells farm machinery in this country, it sells it at a price which it fixes—and it fixes that price, not the farmer. But it uses this device. It keeps up this price, but it dumps its surplus in some foreign country, so that in every foreign country in the world the farmers can buy American machinery more cheaply than they can in this country, which means that American society is subsidzing the harvester trust. That is a fact, is it not?

Mr. Weyforth. I do not know about that particular industry.

Mr. Goldsborough. Well, it is a fact, is it not, that we grant subsidies for carrying the mail to steamship lines and railroad lines, and things of that kind? Society does that, and it is a fact also, of course, that for 100 years we have maintained various tariffs which are artificial means of subsidy. That is true, is it not?

Mr. Weyforth. That is true.

Mr. Gifford. Not subsidy; safety.

Mr. Goldsborough. Safety? Well, of course, it depends a great deal on what section of the country you are living in whether you call it subsidy or safety.

Now, do you consider the various devices that I just mentioned as being unsound economically?

Mr. Weyforth. That is a rather broad question to answer.

Mr. Goldsborough. I know, but you have indicated, and I am not trying to put you through the kind of a cross examination that a lawyer would put a witness through; I am simply trying to direct your attention to situations which now exist——

Mr. Weyforth. I think that Government subsidies may be justifiable if you can accomplish what you want to accomplish with those subsidies.

Mr. Goldsborough. Here is a situation where on the one hand we are told that we must raise the wages of labor. I agree with that. We are also told that we must reduce the price of the articles at retail to the ultimate consumer. Now, those things are contradictory. They both ought to be done, but the one contradicts the other. Whenever wages are raised the prices to the very people whose wages are raised are also raised, the prices of goods at retail, so that they are no better off after their wages are raised than they were before.

Now, one of the purposes of this bill is to attempt to cure that situation. It is an attempt to permit the wages of the laborer to be raised and at the same time to see that the prices of the things that he buys are not raised, so that they will be within his power to purchase. That is one practical result that those of us who are interested in this bill hope will come about without inflation.

Mr. Weyforth. That is a laudible purpose, but I do not see how it can be done. After all, you cannot——

Mr. Goldsborough. You do not think that the reduction of prices at retail would help the masses of the people that are definitely called labor in this country?

Mr. Weyforth. It would if you could reduce prices and find a way for the businessman to operate at a profit, but you cannot in the final analysis hoist wages above the product of labor, and unless the plan increases the product I do not see how you can increase the income of the people.

Mr. **Goldsborough**. You have not been here during these hearings. Of course, the purpose of this bill is not to let this discount come into operation until the goods which correspond to the discount are actually produced and go into consumption, so that under the theory of this bill, when the discount is used, additional goods go into consumption, the idea being that if you increase the amount of goods you produce and consume, at the same time you increase the amount of money in circulation and you are not causing inflation.

Mr. **Weyforth**. But wouldn't you cause inflation here unless you took steps to check it? The bill provides that steps should be taken to check inflation.

Mr. **Goldsborough**. Suppose that we have a 15-percent discount in operation, and a lady goes down town to buy a $10 pair of shoes, and she finds that those shoes, under the operation of this bill, which she knows nothing about, sell for $8.50, and she has a dollar and a half left over that she had intended to spend for shoes, and so she buys a pair of gloves. Hasn't production been increased?

Mr. **Weyforth**. But what has occurred there? This retailer has now obtained a bank deposit of $1.50, and the bank's reserves have been increased by $1.50, and on the basis of those increased reserves the bank credit could be expanded. That is the way you get inflation.

Mr. **Goldsborough**. It would be unreasonable for us to suppose, you not having been present at our hearings, that you are thoroughly familiar with the bill. But, as a matter of fact, that discount money does not get into the reserves at all.

Mr. **Weyforth**. Let me read a section of the bill. I do not understand the meaning of this section (d), which reads——

Mr. **Goldsborough**. That is not said in criticism at all.

Mr. **Weyforth** (reading):

> Interbank currency notes shall be accepted for all forms of Federal taxation payable directly by the banks, and may be used by them as bank reserves, dollar for dollar.

Mr. **Goldsborough**. Dollar for dollar, but not used as fractional reserves, don't you see?

Mr. **Weyforth**. Well——

Mr. **Goldsborough**. It could only be used dollar for dollar.

Mr. **Weyforth**. Wouldn't it release other reserves, so that credit would be able to expand?

Mr. **Goldsborough**. How is that?

Mr. **Weyforth** (reading):

> used by them as bank reserves, dollar for dollar.

Mr. **Goldsborough**. That means the deposits which they could create.

Mr. **Weyforth**. Just how would you distinguish those deposits from other deposits?

Mr. **Goldsborough**. By an ordinary bookkeeping process.

Mr. **Weyforth**. In other words, they would not count these as reserves at all? They would just be assets of the bank, but not reserves?

Mr. **Goldsborough**. That is correct.

Mr. **Spence**. On page 14 it says:

> Nothing in this act shall be construed to prevent the use of open-market operations in Government securities or the readjustments of the discount rate by the Federal Reserve banks in maintaining stable conditions in the money mar-

ket and nothing in this act shall be construed to affect the provisions governing the increase or decrease of the required reserves of banks enacted in the Banking Act of 1935, except that the Board of Governors of the Federal Reserve System shall have the power to increase the required reserves of all national and member banks up to and including 100 percent.

Now, suppose that the reserves of the national banks were increased up to 100 percent; what effect would that have on the banking situation in the country?

Mr. **Weyforth.** Of course, you would not do it at the present time unless you provided the banks with increased reserves; that is, you could not increase their reserves to 100 percent on the basis of their present holdings of reserves. They would have to liquidate most of their loans in that case.

Mr. **Spence.** Suppose that we said so in effect; what effect would that have on future banking activities? What could the bank loan if it had 100 percent reserves was required to maintain 100 percent reserves?

Mr. **Weyforth.** As I understand the theory of the advocates of the 100-percent reserves, it is that under the present system the increase or decrease in the supply of the money of the country depends upon the increase or decrease of the loans of the banks, and that under a 100-percent system, that would not be possible. Banks could not increase the supply of money by increasing their loans, and the supply of money would be adjusted by some Government commission according to some standard, perhaps with an idea of mtainaining stability in prices. I am not sure it should be done, but that, I think, is the theory. It would not be within the control of the banks to affect the volume of money by means of their lending or refusing to lend.

Mr. **Williams.** What is a reserve? What is the purpose?

Mr. **Weyforth.** The purpose of the reserve?

Mr. **Williams.** Yes.

Mr. **Weyforth.** Of course, originally I think the purpose of the reserves was to enable the bank to meet the demands of depositors for cash. I think that there is another idea now, however, back of reserves, and that is the idea of serving as a controlling factor in determining the volume of bank credit and bank loans. For instance, we gave the Federal Reserve Board the power to raise the reserve requirements of the banks. I do not think that that was done with the idea that the existing reserve requirements were not sufficient for the banks to meet all demands made upon them, but it was done with the idea of controlling the expansion of credit. If large excess reserves exist in the banking system we may find great expansion of credit, and if there is danger of too great a volume of credit, one way of controlling that is to raise the reserve requirements of the banks, and then, although they have the same reserves, they can not be used as a basis for credit expansion.

Mr. **Williams.** The loaning power of a bank is not determined by the reserves, but by the excess reserves, is it not?

Mr. **Weyforth.** That is true.

Mr. **Williams.** They do not lend on reserves, do they?

Mr. **Weyforth.** No. Of course, under our law at the present time they are not permitted to increase their loans if their reserves are below the required minimum.

Mr. Williams. And the reserve is there primarily and solely, for that matter, for the purpose of protecting the depositors and insuring the payment of the deposits?

Mr. Weyforth. I think that that is the fundamental purpose; but I think this, too——

Mr. Williams. But then that same idea was back of the other, to avoid loans, undue expansion of credit based on your excess reserves?

Mr. Weyforth. That is right.

Mr. Williams. Over and above the legal-reserve requirements?

Mr. Weyforth. Yes.

Mr. Williams. You do not make a loan at all, legally, if you do not have any excess reserves.

Mr. Weyforth. That is true.

Mr. Williams. If it came out of the reserves it would make your excess fund below the legal requirement.

Mr. Weyforth. That is true.

Mr. Williams. And if you had a 100-percent reserve, doesn't that mean that you would have to keep in your reserve fund dollar for dollar equal to your credit liabilities?

Mr. Weyforth. That is true.

Mr. Williams. And, that being true, what would the bank have to loan?

Mr. Weyforth. Well, under the 100-percent reserve plan, as I understand it, there would be another department of the bank that would do the lending, and this one department that kept the 100-percent reserves would be merely a currency department, for providing currency.

Mr. Williams. What would the other department have to loan?

Mr. Weyforth. Its operations would be like that of a savings bank at the present time, whose deposits would not be used as currency.

Mr. Goldsborough. That would not be similar to this bill.

Mr. Weyforth. No. I do not understand that this bill was intended in that way.

Mr. Williams. I wish that you would point out the difference between the present system and what it would be under this bill, so far as the reserves are concerned. What would be the difference under this bill if interbank currency went into the picture? It expressly says that it may be used for reserves, and that being true, why is it not just the same as our present plant, except of course to furnish additional currency?

Mr. Weyforth. Of course, Mr. Goldsborough says that it is not to be used as reserves. I understood from the bill itself that it was to be.

Mr. Williams. It says that it may be, and I am assuming that it would be used for that purpose.

Mr. Goldsborough. Dr. Weyforth——

Mr. Williams. You understand my question. That being true, if it is to be used as a reserve, what is the difference from that standpoint between that and the ordinary currency?

Mr. Weyforth. I do not see any difference, if it is used as a reserve.

Mr. Williams. I do not either.

Mr. Ford. Mr. Weyforth, suppose——

Mr. **Goldsborough.** Can I ask him a question, please?

The difficulty in this hearing has arisen over differences of definition. I do not think there is the slightest difference between any of us on this 100-percent reserves, except one of us is talking about one thing and another about something else.

Now, under the 100-percent reserve, if we ever had a 100-percent reserve under this bill, and I do not know whether it would be necessary or not, but if we ever had it under this bill, the banks, instead of having a fraction of the amount of money necessary to transact business, would have 100 percent of the money necessary. I will express it in this way:

Suppose that a bank, prior to the time when the reserves were raised 100 percent, had a cash reserve of $100,000, and the banks had the ability to expend to $60,000,000,000 by virtue of their reserve operation, if they used their power to the fullest extent—isn't that true?

Mr. **Weyforth.** You mean the banks as a whole?

Mr. **Goldsborough.** The banking system as a whole.

Then, suppose that this interbank currency became gradually such a part of the banking system as to make it wise for the Federal Reserve System to raise the reserves of the banks to 100 percent. We can presume that at that time the interbank currency would amount to some $60,000,000,000. The bank which I use as an illustration would then, instead of having $100,000 in its reserve, have $1,000,000 in its reserve. That would be the difference. But when it came to making its loans, instead of loaning 10 times $100,000, as it could do under the present law, which would be a million dollars, it could simply loan $1,000,000 based on its 100-percent reserve which it would then have.

So the operation of the bank would be exactly the same.

Mr. **Weyforth.** Then it would have deficient reserves.

Mr. **Goldsborough.** Instead, it would pay its depositors dollar for dollar, if necessary.

Mr. **Weyforth.** Wouldn't it have deficient reserves, then? It has $1,000,000 in reserves, and that was on a 100-percent reserve, and you say it lends $1,000,000. Wouldn't it have deficient reserves, then?

Mr. **Goldsborough.** Let us just change our terminology and say that it would lend it in cash. It does not have to pass the cash over the counter. It can lend the cash by check, of course.

Mr. **Weyforth.** Suppose one bank does that, it——

Mr. **Goldsborough.** Suppose that they all did it?

Mr. **Weyforth.** If they all did it, then their deposits would be increased, would they not?

Mr. **Goldsborough.** How is that?

Mr. **Weyforth.** If they all loaned, then their deposits would be increased. These loans will create deposits. You said before that the reserves were just equal to the deposits. Now the deposits have been increased, and your reserves would be deficient. They would be less than 100 percent of the deposits.

Mr. **Williams.** There would not be any there.

Mr. **Goldsborough.** Not at all. The cash in the banks and the deposits in the banks would be the same and would have to continue the same.

Mr. **Weyforth.** But the deposits would be increased by the loans.

Mr. **Goldsborough.** Oh, no.

Mr. **Weyforth.** If the deposits were not increased, then the cash would be decreased.

Mr. **Goldsborough.** As you make your loan, your cash is decreased. You have a million dollars in cash.

Mr. **Weyforth.** Right.

Mr. **Goldsborough.** And you loan $100,000.

Mr. **Weyforth.** Right.

Mr. **Goldsborough.** Then you have only $900,000 left to loan.

Mr. **Weyforth.** That is right.

Mr. **Goldsborough.** That $100,000 is either redeposited in your bank so as to reestablish your million dollars, or else it has been put into some other bank.

Mr. **Weyforth.** Right.

Mr. **Goldsborough.** But the amount of loanable funds has neither increased nor decreased by reason of that borrowing and depositing.

Mr. **Weyforth.** The amount of deposits has increased.

Mr. **Goldsborough.** I do not agree with you.

Mr. **Weyforth.** I think that I could demonstrate that to you.

Mr. **Goldsborough.** I know you are right if you are going to use a fractional reserve system, but if you are going to use a 100-percent reserve system, you are not right.

Mr. **Weyforth.** But the point is that after you had carried through your operation, you would still have a fractional reserve. What the banks have loaned was——

Mr. **Goldsborough.** Just let me continue this a little bit. We have all been born and raised under this system until we cannot think any other way.

Now, here this bank has $1,000,000 in cash.

Mr. **Weyforth.** In deposits.

Mr. **Goldsborough.** $1,000,000 in cash.

Mr. **Reilly.** Is that in deposits, or made up of stock?

Mr. **Goldsborough.** It is in deposits. Here is another bank that has $1,000,000 in deposits.

Mr. **Weyforth.** And cash as well?

Mr. **Goldsborough.** And cash as well. In other words, the cash is money put in the bank by the depositors. It is money owed by the banks to its depositors, but it is cash.

Mr. **Weyforth.** All right.

Mr. **Golsborough.** And not reserves.

Now, then, somebody comes to this first bank and borrows $100,000, so that this bank has only $900,000 left that it can loan.

Mr. **Weyforth.** But it still has $1,000,000 in deposits.

Mr. **Goldsborough.** No; it does not. It does not have but $900,000.

Mr. **Weyforth.** What became of the $100,000?

Mr. **Goldsborough.** Then the depositor, the one who has borrowed $100,000, takes that $100,000 and deposits it in the other bank, so that this other bank now has $1,100,000 to loan, and the first bank has only $900,000 to loan, but the amount of loanable money in the banking system is exactly what it was before.

Mr. **Reilly.** Is it not a fact that you have only $900,000 in the first bank to cover a million dollars of deposits?

Mr. **Weyforth.** Yes.

Mr. Goldsborough. Oh, no.

Mr. Williams. What happened to it? Where did you get your $100,000 to loan?

Mr. Goldsborough. I take it out of the $1,000,000 I had in this first bank.

Mr. Williams. And that belonged to the depositors.

Mr. Goldsborough. That is correct.

Mr. Williams. Then you take $100,000 away from somebody's deposits. When you do that, don't you still owe the depositor that?

Mr. Goldsborough. No; he has taken it out.

Mr. Reilly. He did not take it out.

Mr. McKeough. You have a note for the $100,000.

Mr. Spence. I would like to ask a question.

Mr. Goldsborough. It does not make a particle of difference. We have been arguing about this thing for a week, and I think we ought to get that settled.

Mr. Spence. I would like to ask the witness a question.

Mr. Goldsborough. Let me complete my statement, please.

You have loaned this man $100,000. Now, he either redeposits that $100,000 in this other bank, or he takes the $100,000 and deposits it in the first bank. If he takes it out of the first bank, that bank simply has $900,000 loanable funds remaining.

Mr. Reilly. But——

Mr. Goldsborough. Wait until I am through.

Then, if he puts it in this other bank, that bank has $1,100,000 of loanable funds, and the amount of money in the banking system remains exactly the same.

Mr. Reilly. That is true, but you destroy your 100-percent reserve.

Mr. Goldsborough. Of course you have not, because this bank that now has $900,000 can only loan $900,000.

Mr. Reilly. But it has a million dollars in deposits.

Mr. Gifford. Doctor, this is a primer lesson.

Mr. Williams. Isn't that your conception of it?

Mr. Weyforth. Yes.

Mr. Williams. Undoubtedly you take $100,000 out of the cash. It is somebody's deposit.

Mr. Weyforth. The deposits have remained the same, but the cash has been decreased.

Mr. Spence. I want to ask you a question.

Here are the regulations of the Federal Reserve System with regard to deposits:

> Every member bank of the Federal Reserve System is required by law to maintain on deposit with the Federal Reserve banks in its district a net balance equal to—

the various percentages. Suppose that it raised, instead of stating the percentages that now exist, the reserve to 100 percent. What would the bank have to loan to its customers, except its capital and surplus?

Mr. Weyforth. It would not have anything.

Mr. Reilly. It would only have the capital stock and surplus.

Mr. Spence. That is right.

Mr. Reilly. And nobody would put any capital into such a bank.

Mr. Ford. I want to make an observation.

On September 30, 1937, the total loans and investments in the Federal Reserve banks and member banks amounted to $31,750,000,000. That is the total. The total deposits in those same member banks were $40,350,000,000. The total reserve was $7,050,000,000. The required reserves were $5,850,000,000.

You would still have $1,200,000,000 of excess reserves that can be loaned, and that would enable them to make additional loans without impairing their present position in the slightest. As a matter of fact, the banks are almost liquid, because they have, in addition to the loans and investments, which we are assuming are 100 percent liquid because of the kind of investments and loans that they have, and they have them in the first place against their deposits; and they have reserves of 7 billions, so that they have $38,000,000,000 of actual liquid assets as against $40,000,000,000 of actual liabilities. That does not take into consideration at all the capital stock, the surplus, the undivided profits, the bank buildings, and other assets that the banks have; they are not counted in this at all.

So, if you will take those and add them up, you will find that the banking system today is probably not only liquid, but plus liquid, as we understand liquidity.

Mr. Williams. Assuming that their assets are all good.

Mr. Ford. Yes; and assuming that their fixed assets, like buildings, and so forth, might only be worth 50 percent of what they are on the books, there would still be more assets in the banks than there are actual liabilities as against their deposits.

Now, I am wondering in my own mind whether or not that liquid operation of the banks is not one of the flies in the present economic ointment. What would be your reaction to that?

Mr. Weyforth. I just do not get the import of your question.

Mr. Ford. We will take a bank in a small town that is just liquid——

Mr. Weyforth. You mean, if it refuses to make loans?

Mr. Ford. If it is just liquid, it has cash against its deposits so that it can pay them at any time it wants to; it can always pay out. It does not make any money, but it will be a liquid bank.

Mr. Weyforth. Yes.

Mr. Ford. And very shortly it will be an impaired bank, because the carrying expenses would eat into their surplus, and the first thing you would have cash only against deposits.

Is it not possible that the present situation of the banks today, in their superliquid condition, is somewhat responsible for the lack of money? The average man cannot get a loan. Small business says that it cannot get loans, and big business either cannot get them or does not need them.

This is a little bit outside of the bill, but do you think we might stimulate the lending of money to industry if we applied to commercial loans a system somewhat similar to what we are applying under the F. H. A., with regulations to cover the character of security, and making the same kinds of safeguards as they do when insuring a home?

Mr. Weyforth. I should be very loath to see a plan of that sort tried. We are going so far in guaranteeing everything that if we begin to guarantee all the loans of the banks, I do not know where we will end up.

Mr. **Williams**. There won't be anything for the bank to do.

Mr. **Weyforth**. No; I am afraid they would make very reckless loans.

Mr. **Ford**. I understand that they are considering something of that kind right now.

Mr. **Weyforth**. Is that so?

Mr. **Luce**. Doctor, yesterday, or the day before yesterday, the President, in a press conference, urged or committed himself to the proposal that the price level ought to be raised. A committee of seven has reported a bill which is on the Senate Calendar contemplating raising prices by inflation.

Mr. **Goldsborough**. That is, wholesale prices.

Mr. **Luce**. Wholesale prices?

Mr. **Goldsborough**. Yes.

Mr. **Luce**. There is before the House, with some degree of pressure, a proposal to enact the substance of the Townsend plan, which might involve a great increase in credit, because if money is to be put into the hands of the aged to be dispensed, it must be raised either by taxation or by bonds, the probability being that it would have to be done by bonds.

We are confronted with a variety of proposals to add to purchasing power in one shape or another, and some of us are very much perplexed as to what particular type of proposal shall be followed, that of the President or that of Senator Thomas, or that of our good friend Goldsborough, or one or another of the numerous proposals that are before us.

In trying to think them through and get down to the bottom of all of these proposals, I am confronted and perplexed by the element of what I choose to call artificial capital; that is to say, symbols of purchasing power, and we call them bonds, or notes, or whatever they may be, which are not based upon an equivalent amount of tangible wealth.

Will you help me in my own dilemma, sir, by giving me your view as to the relation of intangible wealth, namely, notes, contracts, and obligations, to this subject? Is it possible by any device to add to purchasing power by the use of artificial capital?

Mr. **Weyforth**. Of course, we know that these forms of intangible wealth that you speak of, notes and bonds and such things, do not in themselves add to actual wealth. I can conceive of circumstances where it is desirable that there should be an expansion in the monetary supply. The great problem, it seems to me, is to know just how far that expansion should go. That, of course, is the problem that confronts the Federal Reserve Board or the credit authorities in any country where a managed currency exists. If you are going to have more money, and there may be circumstances where it is desirable, the question is how much more. There are many proposals made as guides for that purpose—stabilizing the price level, and so on—but the difference of opinion is so great among the experts that one, it seems to me, can sympathize with the credit authorities who are trying to do their duty and who are confronted with the dilemma of knowing just what volume of money in circulation there should be. I do not think that any formula has yet been devised, and so we are driven to a policy of judgment. The credit officials exercise their judgment. They consider that perhaps there ought to be a little easier credit, or perhaps that credit ought to be tightened up a little bit, and they take a great number of factors into consideration, but they have not as yet worked out any formula that is a complete guide to them in determining what their credit policy should be. That, I think, is one of the most difficult economic problems that confronts this country or any country at the present time.

Mr. Luce. Well, does your study lead you to think that the attempt to regulate the creation of artificial capital by legislation is wiser than to leave it to the ordinary operations of the law of supply and demand?

Mr. Weyforth. Under our defective knowledge, I would be more inclined to leave it to the operation of the law of supply and demand. I am not, however, one who believes in a complete policy of laissez faire, and there may be circumstances under which it is desirable to increase purchasing power. I think, for instance, that a certain amount of public works as a means of increasing spending may be desirable. It has not accomplished very much so far, however, in the way of bringing about permanent improvement.

Mr. Luce. I want to go a step further, in order that your position may be made clear, and ask you whether or not you think that artificial capital is not inflation.

Mr. Weyforth. I am not quite sure that I understand what you mean by artificial capital.

Mr. Luce. That which is not fact or represented by tangible wealth.

Mr. Weyforth. You mean Government bonds?

Mr. Luce. Government bonds, particularly.

Mr. Weyforth. It depends upon the way in which the bonds are sold, I should say. If they are sold to individuals who buy them out of their savings, it need not lead to inflation; but if they are sold to banks and create additional deposits, it may.

Mr. Luce. Apply it to the pending bill or to the Townsend plan, either. This proposal contemplates the creation of a volume of interbank currency which is not represented by tangible wealth. It is a promise of the Government to pay, precisely the same as a number of other promises to pay.

Mr. Weyforth. I think that is true.

Mr. Luce. That being so, do you think it makes any addition to the wealth of the country at the moment?

Mr. Weyforth. I do not think so.

Mr. Luce. And it is one of the credit inflationary proposals with which we are faced?

Mr. Weyforth. I think so.

Mr. Crawford. I would like to ask the doctor a question.

You dropped a remark a while ago that I want to go back to. In speaking about what the banks could loan under a 100-percent reserve, did you mean to say that they could not loan their time or savings deposits?

Mr. Weyforth. They could. As I understand the plan, the bank would be separated into two different departments, and in the savings department the loans could be made.

Mr. Crawford. So, then, summing up, they could loan, in addition to what you said, capital, surplus, and undivided profits, savings represented by time or savings deposits?

Mr. Weyforth. That is right.

Mr. Crawford. One other question, and I am through.

When you speak of wages not being able to be increased above the productive labor, do I understand you to mean that wages come out of production, and not from profit?

Mr. Weyforth. Come out of production, I should say.

Mr. Crawford. The reason that I raised that question is that I have had many people tell me in the last 4 or 5 years that wages are paid out of profits, and not out of production. I agree with you. Many people in this Congress are insistent that wages are paid from profits instead of production, but I cannot agree with them at all.

Mr. Williams. Ultimately profits come from production.

Mr. Ford. Service wages come from profits, because if I am giving a certain kind of service to a man, I take into consideration what the cost of rendering it is, and what wages I pay in connection with the rendition of it. That is not true in industry as a rule, but it might apply to services.

Mr. Goldsborough. Dr. Weyforth, we appreciate very much your coming.

Mr. Weyforth. I have enjoyed being here.

Mr. Goldsborough. We have profited very much by what you have said, indeed.

The committee will meet tomorrow morning at 10:30.

(Thereupon, at 12:25 p. m., an adjournment was taken until Friday morning, February 18, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

MONDAY, FEBRUARY 21, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:40 o'clock a. m., Hon. T. Alan Goldsborough, presiding.

Other members of the committee present: Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Transue, Mr. Luce, and Mr. Crawford.

Mr. Goldsborough. The committee will come to order, please.

The committee has as a witness this morning Maj. L. L. B. Angas.

Major Angas, the committee would be very glad to have you state your economic background before you proceed. You do not have to be modest before this committee.

STATEMENT OF MAJ. L. L. B. ANGAS, INVESTMENT CONSULTANT

Mr. Angas. My economic background, sir, is that since 1919 I have been a student of the problem of unemployment. I have written nearly 20 books or pamphlets on the subject of trade fluctuation, particularly concerning its monetary causes. I have visited numerous countries, studying their particular conditions, and have as a result of my studies come to certain conclusions as to both causes and possible cures. I agree that what is true of one country and one banking system is not necessarily true of all, but there are so many similarities of general trade fluctuation that I think it is possible to enumerate a series of economic laws or probabilities which apply to all countries, although each country has minor exceptions.

My business is to act as an advisor to companies and investors, which requires a continuous study of trade fluctuation. I have been a stock broker, and I have acted as advisor to banks in England, and am now an investment consultant.

Mr. Goldsborough. Now, Major, would you prefer to proceed in your own way until you conclude and then have the members of the committee ask such questions as they would like to ask, or would you like to have questions asked during the progress of your statement?

Mr. Angas. With your permission I would like, if I may, to state my own views, and, when that has been done, if the committee would care to question me upon my own views on the general problem of the cycle and of the bill in particular, then I would gladly attempt to answer.

Mr. Goldsborough. You may proceed in that way, sir.

Mr. Angas. When this bill was first sent to me, I glanced through it quickly and put it to one side, rather expecting it to be of a character similar to so many other intended cures for trade slumps, and I expected it to contain numerous fallacies in relation to how the trade cycle may be cured. When I had time to study it more carefully, which I did, I found that it contained what appeared to me to be a very practical method of dealing not only with this slump, but with slumps in general. It struck me as being a bill to adjust the demand for commodities in general to the available productive capacity.

The great western countries have virtually solved the problem of production, but have not yet solved the problem of consumption or distribution in relation to potential production. Today it is perhaps the greatest economic problem of the world. Indeed, an invention is required, something to come from the human mind. The problem is not production; it is consumption, and that should be simple, but it has puzzled the great economic brains of the world for at least a century. No doubt the invention required to balance consumption with potential production is findable, and I think it will prove more useful than the inventions of Edison, Marconi, and Ford. This bill, in my view, contains elements which will get us nearer to that ideal.

At present, in order to cure a slump in underconsumption or overproduction, or, if you like, in enlarged inventories, the process is normally to reduce production and make the world really poorer in order that it may once again get into gear and go forward again and become once again richer. There is something ludicrous about the process, although it seems to be at the moment the only process which works.

Cures have been suggested for the general problem by people all over the world. There are two parties, the orthodox and the unorthodox, or the conservative and the crank. It would appear, judging from the recent economic history, that very often orthodox opinion contains as many fallacies as do the suggestions of the unorthodox and the so-called cranks. Most people desire to be considered orthodox, but orthodoxy, as proved by history, is frequently wrong.

To give a few examples: 300 years ago, in 1635, Galileo, who said the earth went round the sun, was banished from the Italian bishopric in which he lived, because his views were unorthodox and contrary to the teachings of the Church at that time and therefore subversive. We now accept as obvious the then unorthodoxy of Galileo.

As another example, I was in Berlin in December 1922, while the German mark was being inflated. It had then been inflated only 10,000 times. An outcry was growing in the press on account of the rising cost of living and the low purchasing power of the interest on Prussian bonds. The outcry, of course, came from pensioners and all Government officials with fixed salaries. The then head of the Reichsbank was Dr. Haverstein, the Reichsbank being one of the greatest central banks of the world. He was attacked for the note inflation. His defense was, and I speak from memory, but I think a perusal of the columns of the Berliner Tageblatt of December 1922, will confirm me in what I believe to be an accurate memory—his defense was that the rise in prices was not due to the increased quantity of paper marks; in fact, he said that he was only satisfying the demands of the great commercial banks, the 4-D banks, as they are called, and that if he did not supply them with the paper money that they asked for, for the conduct of the trade of the country, that trade would suffer, and that therefore it was his duty to increase the supply of marks according to the demand of the big four German banks. He said, in fact, that money had nothing to do with the price level. It was not the dog which wagged the tail, but the dog which was wagged by the tail. He further added that the real cause of the rise in German prices was scarcity of commodities consequent upon the war and the peace treaty, coupled with wicked foreign speculation in the German mark, which had depressed it out of the foreign exchanges, and therefore made imports more expensive.

There, gentlemen, was the voice of orthodoxy and the voice of authority. He had, no doubt, been brought up to believe that money was merely a madium of exchange, and here I quote Adam Smith, "which had no influence upon trade itself, but was merely a passive factor and not an active factor either on prices, or industry, or employment." I quote that from Adam Smith, in Wealth of Nations.

Another instance. Mr. Walter Leaf, formerly chairman of the Westminster Bank, in London, one of the Big Five, stated in writing that banks could not create credit. In my own country, again, Dr. Cannon, Senior Professor of Economics at the London School of Economics, stated—and I have heard him say it myself—in the early twenties that banks could not create credit. I have heard Dr. Benjamin Anderson, economist to the Chase Bank, say so in 1935.

On the other hand, other leading bankers, like Mr. McKenna, of the Midland Bank, and all of those who gave evidence before the McMillan Committee on Currency, said that banks can create credit.

But men of high reputation and authority, following the orthodox view, are not always reliable as regards the practice of applied economic theory.

In my own country, in 1931, the National Government was formed to save the pound. The country was placarded with notices asking votes for that Government in order to save the pound and prevent inflation, because a devaluation of the pound and monetary expansion were regarded as the road to ruin, and as causes likely to increase the then-existing slump. As it happened, within 3 days of the formation of the National Government, on September 21, 1931, the pound fell in value, which slightly improved trade, particularly the export trades, and then 8 months later, when the war loan was converted, an expansion of credit began, and from the date of that credit expansion, English trade recovered. Bank credit currency has been inflated 21 percent in Great Britain since that date, and the country has been continuously prosperous until the American slump began last August.

My reason for citing the question of orthodoxy and the views of accepted authorities is to suggest that the views of the textbooks on the subject, or of the greatest men at the head of the administration of a problem, are not necessarily right.

This bill, Mr. Chairman. I think, will be attacked in the press throughout the world with four adjectives, and these adjectives will be that it is unorthodox, that it is unsound, that it is artificial, and that it is inflationary, and if the opponents of a bill can tie these labels around its neck, they will probably strangle it. I am, therefore, having had 15 or 20 years' experience with problems of monetary reform, not very hopeful that any bill aimed at adjusting general consumption to general productive facilities will meet with success, except in the deepest crisis period.

Unorthodox! A thing is unorthodox if it is not in accordance with what has been recently taught, and, in the economic field, taught by professors. A thing is unsound, similarly, if it is not in accordance with orthodox teaching. A thing is artificial if it is not in accordance with the natural forces of the day. Incandescent gas, electric light, inoculation are all artificial, but are not necessarily bad. They may be an improvement on nature, on darkness when it is not wanted, on smallpox, and so forth. The word "inflation," or "inflationist," is a happy bowl of mud to throw at anyone. It sticks. But inflation is a word which has 22 meanings to me. For instance, there may be inflation of gold, or of notes, or of bank credits. There may be an inflation of retail prices, of wholesale prices, or of costs. There may be an inflation of profits, and so one can go on. There can be, in fact, a blowing out or up of anything.

This bill is inflationary in the sense that it aims at inflating or reflating or expanding consumption in relation to production. It may also be inflationary in that it augments the volume of money in circulation. It may also be inflationary in that it increases wages and the general welfare. The word "inflation," in fact, is a meaningless word when undefined, but it is a good bowl of mud to sling at people, because not everyone will analyze the sense in which the expansion or inflation of something occurs.

To eat is good. To overeat is bad. To expand money parallel with trade is good. To overexpand money, as in Germany in 1922 onwards, is bad. Eating and overeating are both putting things in one's mouth, but it is the amount that you put in which matters. It is desirable to put a certain amount in, to get the right balance for one's health, but to put too much in, or to put too little in, is gluttony or starvation.

But this bill will doubtless be attacked on the ground that it is unorthodox, unsound, artificial, and inflationary.

But I am not concerned with the popular methods of killing or strangling measures aimed at improving national and world welfare. I am concerned in finding cures which will eliminate the diseases without creating even greater diseases, and in order to assess the merits of this bill, it seems necessary to me to analyze the diseases of capitalism which give rise to the trade cycles and the recurring unemployment of machinery and men.

Unfortunately, the trade-cycle problem is complex. No two trade cycles are exactly the same. They have never been. They have similarities. They have different sets of causes, and any one omnibus cure is probably inapplicable to all the trade cycles of all countries for all time.

There are several diseases of the human body. There are several diseases of the economic body. Reading this bill through, I find it to possess qualities which will deal, in my view, with most trade cycle diseases. I did not say all—I said most. It is not a panacea, but its adoption, or the adoption of other bills with similar features, will, I think, prove ameliorative. Indeed, I would describe the bill as one aimed at enhancing wages and profits, a bill, in fact, which will prove of benefit to both workers and businessmen, and will also augment the safety of the fixed incomes of pensioners and persons who live from a fixed money income. I say that because this bill will tend to prevent fluctuations in the general price level at the same time as it tends to augment consumption in relation to productive facilities.

Now, let us look at the normal business cycle, or the so-called credit cycle which has been the feature of Europe rather more than America since the bank credit system was developed from 1844 onwards. It was called the credit cycle, because its chief factor was a cumulative expansion of credit during periods of prosperity, which added fuel to upward price movements, eventually culminating in a boom, whereas on the down side, as business contracted and prices fell, credit was contracted even more, so as to add a cumulative downward momentum to the slump.

In other words, the natural working of the banking system, which is a system whereby money is issued against loans, collateraled by commodities, was that when things were rising, the banks lent more, because it was safer, and the higher things went, the more they lent, because values were increasing and each loan became safer, or, as the bankers called it they lent on the quality theory of credit.

But it always led to trouble in the end, because of the feature of the banking system known as the cash reserve ratio system, which meant that as you expanded credit progressively, and as prices and wages rose, two diseases gradually hit the banking system. Eventually credit became expanded until the reserves could stand up no more, according to the ratio system, and at the same time cash started flowing out into general circulation from bank reserves to finance higher wages and more retail trade at a higher level of prices, and eventually credit strain developed, owing partly to the expansion of credit and partly to the flow out from the banks of their reserves into the general form of cash. That is the business cycle, normally, that is how a boom culminates, by money strain or credit strain, and fear develops nervousness, banks call in loans, forced sales occur, prices fall, and other banks call in loans, because prices are falling, and so there occurs a cumulative downward deflation.

There is a natural cure, Mr. Chairman, which results from prices and the volume of trade falling to such low levels that the credit structure of the banks is reduced. This is the natural cure. At the same time wages, retail trade, and retail prices fall to such a low level that cash returns from general circulation into the banks, so that their reserves are increased at the same time as their outstanding loans are decreasing. The banking position, therefore, tends gradually to strengthen, and after a period of years the credit structure becomes sound again through the country going through what is called the ringer, and at last curative forces in the monetary machine begin to reassert themselves, because the banks again are so strong that they augment their investments, which puts money into circulation again, reflationary money, and that slightly improves trade and then business borrowing begins again.

That is the natural process, and if one believes in artificial interference in the business cycle, one must expect continued recurrences of these trade cycles which result not from some error on the part of any man or government, but from certain features in the banking system, namely, the cash reserve ratio system and from prudent banking itself. A prudent banker will lend more if more collateral is offered to him in a rising price period, which tends to inflate prices still further. During a falling trade, the prudent banker in the course of his duty toward his depositors and his shareholders contracts credit as prices fall or as the outlook deteriorates, thus making trade worse. So, prudent banking is one of the influences on the cumulative swings downward in the business cycle. It is nobody's fault. It is inherent in the banking system which has grown up out of past history.

Mr. FORD. When you have completed your remarks, I wonder if you would answer a question, which is just what was the basic reason for the German inflation? I have read several——

Mr. ANGAS. I will answer it now. It began during the war, because the Government could not tax quickly enough to pay for the financing of the war.

Mr. FORD. But it ends up with their not being able to raise taxes quickly enough to pay for the commerce that they had to send to other countries, in the form of reparations?

Mr. ANGAS. It is a very long history to describe. It began because the Government could not collect taxes fast enough to finance the war while it was going on. Then that involved borrowing by the Government from the Reichsbank and from the other banks, and they have a note system rather than a depositor-currency system, and that led to the inflation chiefly of notes, and slightly of deposits. That started a mild rise in prices, and then businessmen and speculators started borrowing, and since they could offer the collateral, the banks lent more, and that inflated prices again, and that sent up Government expenses faster than tax revenues came in, because there is always a lag, particularly in the German method of tax collections, so the Government had to borrow still more, and that put prices up, and then the people borrowed more, and the Government borrowed more, and it went on and on until the mark went to 300 trillions to the pound.

I do not think that they did it deliberately. They got in an avalanche. I do not think that it was in order to cheat the foreigners. They cheated the Germans at home more than the foreigners.

Mr. FORD. Then they had to supply a certain amount of gold.

Mr. ANGAS. That was part of the Government's debt.

Mr. FORD. Wasn't that a factor in their inflation?

Mr. ANGAS. Yes; it was part of the German debt, and they had to pay it with some sort of money to send the coal and other things to France and Belgium, and they created the money out of nothing.

Mr. FORD. And they could not collect taxes fast enough to make it good?

Mr. ANGAS. That is right.

Mr. GOLDSBOROUGH. Now, gentlemen, some of you were not in here at the beginning of Major Angas' statement. He said that he preferred to complete his statement, and he would be very happy to answer any question that he was able to answer.

Mr. ANGAS. Mr. Chairman, may I go on and develop this a little bit?

Mr. GOLDSBOROUGH. Go right ahead, sir.

Mr. ANGAS. What I have said so far was a preamble, rather. I will now attempt to look at the causes of bad trade from another angle. If there were time, one might well discuss the fundamental possible causes of a reduction in trade under a barter economy, where the money factor did not enter at all. I am aware of some of those factors, which depend mainly upon the satisfaction of human wants or the absence of human wants, coupled with inefficient production and other such nonmonetary factors. But I will pass over that and merely mention it to show that I have not forgotten the possibility of trade being bad for other than monetary reasons.

In terms of money, bad trade, to use simple language, results from people not spending money fast enough on goods and services, and any general check to this flow of money onto commodities may be due either to something physical occurring or something mathematical occurring in the sphere of money itself or even in the sphere of commodities, or, alternative to something mental as distinct from mathematical going on in the minds of the people who own money and who might spend it but do not. That is all that bad trade is.

As regards the volume of money, changes in the volume of money can act as the cause of bad trade and possibly as a cure to bad trade.

Let us look at changes in the supply of money as an influence of trade, including profit and employment. Obviously, inflation and deflation of the total supply of money influences trade and employment, for if you multiply the volume of money, say, tenfold, more of it gradually gets spent on goods at the old level of prices until trade, with a time lag, becomes so good that the inventories fall so fast that profits, prices, and employment all rise.

Conversely, if the total quantity of notes and bank credits is deflated as they are being today in America to the tune of 6 percent since last December, less money is spent on commodities at the old level of prices, and trade, profits, prices, and employment all decline.

It is in this specific way that inflation and deflation, whether accidental or deliberate, influence trade, employment, and profits, with a time lag. Small amounts of inflation and deflation may have little effect, but progressive inflation invariably catches, as also does progressive deflation. Unfortunately, in the last 12 months in America, there has been an accidental 6-percent deflation of bank deposits due to the banks selling bonds through fear of a rise in the rate of interest—that is the chief cause—and bank credit in this country has been deflated by one and a half billions in the last year, and this is one of the causes of the present slump.

But there is another monetary factor—it has nothing to do with the volume of money—which also affects trade, namely, the velocity of money, which is largely governed by confidence and fear, although I must admit that velocity is also influenced by prospective and actual changes in the quantity, and this is where the bill under discussion becomes important. The amount of money that is spent on goods and services for, say, a year depends not only upon variations in the total quantity of money, but also on variations in its average velocity of turn-over.

As regards velocity, obviously if half of the money in existence is hoarded, say through fear, and kept idle, say, for 20 years, to take an extreme case, this 50-percent decline in average of velocity is equivalent in its effect on actual business to a 50-percent deflation of the actual total quantity of money, and it is largely on account of a 15-percent decline in the velocity of money in the last 12 months, due primarily to fear, fear of this and fear of that and fear of another thing, and I am reluctant to mention all the current fears at the moment, but they exist—it is largely due to this 15-percent decline in the velocity of money that the present so-called mystery or confidence depression has resulted.

In other words, from a monetary point of view, there may be two causes of bad trade, a change in the volume of money or a change in its velocity, due to fear. But velocity can change for another reason, namely, confidence. The change in confidence, or hope about prices, is an important influence on velocity. If prices are expected to rise, men will rush in with idle money and buy. That improves trade. It may force prices up. That may improve profits for a second reason. Thus velocity is influenced not only by political and economical fear, but also by expectations concerning coming movements in prices, and insofar as a prospective change in the volume of money can cause an anticipated change in the price level, it will directly affect velocity or the speed of spending temporarily hoarded money. Indeed, a threat of inflation may cause an improvement in trade, without any inflation occurring, actually. That happened in this country in 1933. The true inflation of volume of money did not begin until 1934.

This question of velocity, though usually neglected because of its complexity, is of vast importance to every man and woman in the world. Indeed, the great economic feature of the post-war period is the influence of fear on prosperity. Since the war began, all rich men and all poor men in all countries have become nervous. There is a world revolution going on, in human thought, in industrial technique, in taxation methods, in forms of government, and nobody knows what is going to happen next, because these changes are going so fast, and men are frightened, and a frightened man who is in possession of money is a dangerous man socially, because he takes money out of circulation through fear and keeps it idle, because he does not know what is going to happen. He does not spend it at the normal speed.

Therefore somebody else goes without what might be called a normal income. That second group suffers, and, when it begins to suffer, it becomes frightened, too, and behaves in a similar manner. They spend less. They try to increase their liquid balances of money, idle balances. A third group suffers, and so the process goes on in a cumulative manner, due to a psychological factor.

Now, in America, in the last 3 years, the quantity of money has been reflated some 30 or more percent—I mean bank money, bank credit currency; and yet there has not been very wild inflation, nor has there been a very wild trade boom, and the reason, in my view, is that although the quantity of money was being inflated by Government borrowing from the banks, certain other events—laws, speeches, some governmental, some not—have augmented the fear of not only the rich but also the poor, so that money has been hoarded in America just about as fast as the quantity has been inflated. This is the cause of the great inflation forecast by Dr. Kemmerer, the cause of it not having caught as yet in any appreciable degree; and, sir, I am not as far away from the subject matter of the bill as may appear at the moment, if you will permit me.

Granted that hoarding through fear is an economic disease; granted that it causes unemployment; granted that it is necessary to alleviate unemployment and, if possible, prevent it in the future, it seems to me, as a would-be practical person, that something must be done to solve this problem of hoarding. Unfortunately, the hoarding factor is not a constant factor. Fear fluctuates. Sometimes it will begin a discord; then changes occur, which makes for rehoarding, and trade in consequence fluctuates.

If you believe in complete liberty of the individual, or partial liberty of the individual, you must agree that the invididual has the right to hoard for as long as he likes any money that he receives or earns, but if you wish to keep industrial prosperity on an even keel, and to keep consumption up to productive facilities, it seems to me that something must be done to combat this natural disease. You cannot eliminate the post-war fear, as we are in a world revolution. This disease is a monetary disease, investing in money; it is an increased demand for money for liquidity purposes, and if you believe in the law of supply and demand, you will believe that if demand increases very rapidly, no matter what the reason, supply should be increased to meet the demand as long as the price of the thing demanded shows signs of rising.

When the fear demand for money, or the hoarding demand, increases, money stops flowing and prices fall, commodity prices fall, and, with a lag, labor prices, which is only another way of saying that the economic price or the real price of money itself is rising. And when the real price of money rises—aye, when commodity prices fall—the supply should be increased in accordance with the law of supply and demand.

This bill contains in it a method of effecting that adjustment—artificially, yes; wisely, yes; very wisely, yes, because if nature is left to itself, instead of the supply of money increasing when the hoarding demand increases and commodity prices fall, it is positively contracted, and that is the one dominant feature of the modern banking system, namely, that at those moments when an increase in the supply of money is theoretically and practically most necessary—aye, when commodity prices begin to fall—the supply, instead of being increased, is positively contracted, because bankers, in the course of their duties toward their depositors, must call in loans which they have out, which makes things worse.

Wherefore the modern business cycle; wherefore the growth of new parties, advocating a change in the capitalistic system, and they may be Socialists; they may be straight Socialists, or guild Socialists, or the Russian system, or they may be for control of the totalitarian state, but they are all aiming at curing an economic disease which is nobody's fault. I do not say that they are led by unwise or vicious men; they are led by disappointed men, who are trying to do something, trying to satisfy the hunger of the submerged third.

It is only a matter of brains to me to cure this problem which is inherent in the modern system. All one needs to do is to look at the natural diseases of capitalism and banking. I think capitalism is a splendid system. I think the banking systems are splendid, but they have a few inherent or natural faults which can be cured or will be cured some day, but they require artificial intervention because the causes are endemic or natural, and yet, if you get up and suggest an artificial intervention, you are told that you are unsound, that you are unorthodox. Nevertheless there is a fear complex governing the world leading to the hoarding of money, and yet if you wish to obey the law of supply and demand and increase the money supply in relation to this natural demand resulting from post-war fear, you are called an inflationist, and that implies that your mind does not work, or, if it does work, it works in the wrong direction—in fact, that you are a crank.

Mr. FORD. Doesn't that arise from a misconception of what the function of money is?

Mr. ANGAS. Entirely. It arises from errors in the teaching in the universities of the world. There is not, to my knowledge, a single book which emphasizes the nature of this curious hoarding demand for money.

Mr. PATMAN. Who is responsible for the selection of these teachers?

Mr. ANGAS. It grew up, just like people before Galileo grew up. They said, "Don't be a fool, Galileo. Can't you see that the sun goes round the earth? Be practical. You see it every day. It is crazy to say that the earth goes round the sun, when you can see the reverse happening. What you want to do is to be a practical man, not a theorist."

That is how this mess of capitalism has developed. They are taught to believe certain things, just like the people of Galileo's time were taught to believe that the sun went around the earth. It seemed obvious. The other theory just was not true. It was a delusion, just like the delusion that money is not wealth, that is is merely a medium of exchange and has no influence on wealth itself.

Now, let us get on to cures. From a monetary point of view, bad trade can result either from there not being enough money, or from its being hoarded. It may also result from its being maldistributed between different classes, but that is a complex subject which I do not intend to discuss in this evidence unless pressed to, sir. Either there is not enough money, or it is hoarded. Those are the two chief causes.

Mr. McKEOUGH. Might I interrupt?

Do you consider the maldistribution of profits a major factor?

Mr. ANGAS. Yes; at times.

Mr. McKEOUGH. That is all I care to ask now.

Mr. ANGAS. It was very serious in the autumn of 1929. It is somewhat serious at the moment, wiping out the hoarding problem which also exists at the moment.

In 1928 and 1929, wages were not getting quite enough, in my view, of the national dividend, when it was growing so fast, and at the moment now that the slump is here, many rentiers, people with fixed incomes, are getting too much of the reduced national dividend, but I will come to that point when I discuss the profit question later.

Theoretically, of course, if you will grant me that there is a fluctuating hoarding demand for money, and that the supply of money should be increased when the price of it rises, as represented by a fall in commodity prices, I think you must also agree that an artificial factory of money is required, increasing the supply of money as prices fall unhealthily, and if the corrective action makes prices rise unhealthily afterwards, to contract the supply once more.

Indeed, the philosophy of managed money is similar to that of driving an automobile along a narrow country road, with ditches on either side. If the car swings too much toward the ditch of deflation on the left, if it swings naturally in that direction, it is essential that the driver, or money manager, take such action as will swing it away from that ditch, more toward the middle of the road, but whether you like it or not, it is a fact that corrective actions aimed at avoiding the ditch on the left point the car toward the ditch of inflation on the right, so that when it gets to the center of the road it will naturally in all probability, unless some other factor or bump intervenes, proceed toward the ditch of inflation on the right, which requires that the chauffeur should turn the steering wheel the other way.

Indeed, the art of driving a car along the center of a road with dangerous ditches on either side, is to fiddle continually with the steering wheel with light fingers, or to monkey continuously with the peoples' money, or to interfere with the bankers, and yet if you say these things, you are attacked for wishing to interfere in private industry, or for wishing to augment the amount of Government management, or you are even attacked for wanting to set up an institution which will cost the Government still more money and therefore raise taxes. You will be attacked particularly on the ground of interference with a managed economy.

From my writings, if any of you have read them, you will gather that I am not in favor of a managed economy, because in a single industry overproduction corrects itself through a fall in price, which stimulates demand, so that demand and supply become naturally equated.

Similarly, underproduction leads to a rise in price, which stimulates extra profits, and which corrects the underproduction. Indeed, management in single industries is not necessary in the long run, because in the long run the automatic natural forces effect the correction, but in banking and in money, it is just the reverse.

Mr. TRANSUE. Do you include agriculture there?

Mr. ANGAS. Yes, sir. Money is different because a rise in price or fall in commodity price leads to a contraction of money. That is why I want to see money managed, although I do not, as it happens as an individual, with my own predilections, want to see other industries managed. Indeed, managing money to me is a method of eliminating the cry for management in other industries, because if you manage money properly, you will not have very many cries for managing anything else, and in this bill lies a method, not the only method, but a method.

Now, sir, you raised the question of profits and the redistribution or the maldistribution of money income as a cause of bad trade.

Mr. GOLDSBOROUGH. Major, could you return tomorrow morning?

Mr. ANGAS. Yes.

Mr. GOLDSBOROUGH. The House is in session, and some of the Members desire to be on the floor. So, if you can come back tomorrow, the committee will now adjourn until half past 10 tomorrow morning.

(Thereupon, at 12:02 p. m., an adjournment was taken until Tuesday morning, February 22, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

TUESDAY, FEBRUARY 22, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:45 a. m., Hon. T. Alan Goldsborough presiding.

Other members of the committee present: Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Transue, Mr. Barry, Mr. Luce, and Mr. Crawford.

Mr. Goldsborough. The committee will come to order.

Major Angas, will you proceed in your own way, please, sir?

STATEMENT OF MAJ. L. L. B. ANGAS—Resumed

Mr. Angas. Mr. Chairman, I attempted yesterday to point out those inherent features of the capitalistic system and the modern banking system which automatically and naturally give rise to trade fluctuation, alternate booms and slumps, not because of anyone's fault, but because of the nature of the banking and capitalistic system which we in our generation have inherited from the past.

I pointed out that the cash reserve ratio system of banking, and the fact that the wage earner and retail trade used a different form of currency, namely, legal tender, a different form from that used by the business of the country and the relatively rich, that that factor led during prosperity or rising prices to a drain of cash from the banks into public circulation at the same time that they were expanding credit, until eventually credit strain matured, coupled normally with high interest rates, and when prosperity or prices came to the end of the tether, there was a tug which created fear, and then a back swing, and I suggested that some form of adjustment of the supply of money to the demand and some artificial interference so as to eliminate these natural and inevitable swings might be desirable.

I further added yesterday that quite apart from these inherent or endemic diseases in the banking system and in the capitalistic system of today, there was the additional problem, a monetary problem, of the ever-varying demand for money, and I mean by that idle balances on the part of the people who may from time to time become frightened and, through their fear augment their liquid balances of money, refuse to spend them with a normal speed, and create bad trade because they keep that liquid money out of active business circulation, thus virtually doing a thing which is tantamount to a quantitative devaluation of the total supply.

Mr. Ford. Might I ask the major if he detected that situation existing in 1929?

Mr. ANGAS. The fear complex?

Mr. FORD. Yes.

Mr. ANGAS. If anything, just the reverse. Indeed, the amount of hoarding or investing in money in 1928 and 1929, during the new era mentality, was abnormally low, in my view. People were so confident both about business and the value of money that they probably reduced their amount of hoarding below normal. In other words, you had reverse conditions from today.

Mr. FORD. That is, the amount of money in circulation was very low?

Mr. ANGAS. It was very effective, and when some slight fear came along, then we got in some degree the diseases of today, a vast amount of hoarding as soon as fear enveloped the Nation in 1929.

Mr. FORD. The thing that I am trying to develop is that the thing that you call circulation of money is a mere fallacy as far as actual money is concerned. I do not mean credit; I mean currency.

Mr. ANGAS. I do not quite get the purport of your question.

Mr. FORD. I will tell you why I ask that question. At the depth of our depression in the United States, the volume of money in circulation, so-called, was at its highest peak in years.

Mr. ANGAS. Of legal-tender money?

Mr. FORD. Yes; in circulation.

Mr. ANGAS. Yes.

Mr. FORD. What I am trying to get at is, what was your observation in 1929 as to the character of that money? How much of it was there, as you remember it?

Mr. ANGAS. Do you mean statistically?

Mr. FORD. Yes.

Mr. ANGAS. I have forgotten the figures.

Mr. FORD. It was very low, was it not?

Mr. ANGAS. Yes, sir.

Mr. FORD. And in the depth of the depression, very high?

Mr. ANGAS. Yes.

Mr. FORD. I just wanted to develop that for a later question.

Mr. ANGAS. In the very depths of a depression, I think that people will be afraid of the banks, which of course makes the banks shakier. When confidence in the banks declines, the fear of the banks increases. It is a subtle thing. Fear of the banks leads people to hoard notes and take them out of the banks, and fear of money makes them dishoard money, try to pass it on, a subtle difference, but it is one of the four chief types of confidence.

To go back, the second point that I made was that quite apart from the endemic diseases in the banking system which created a trade fluctuation, inevitably there was this extra problem of fear, causing hoarding, which has nothing to do with faults in the banking system of an endemic nature, and if you have much of it, it may be desirable to manipulate the supply of money and satisfy the varying liquidity or hoarding demand.

Now, holding those views, as I do, I am inevitably in favor of some form of managed money, of adjusting the supply to the demand, both the hoarding demand and the business demand, and the curious thing is that when the business demand for money, or medium of exchange demand for money, declines, owing to worse trade and to falling prices, the other sort of demand, namely, the hoarding demand or store of value or liquidity demand, increases, and that is the most unrealized feature in the realm of monetary thought, in my view. Most economic writers on money never mention that as the medium of exchange demand declines, it is almost always the case that the store-of-value demand for money resulting from fear increases even faster. That is a subtle characteristic of the demand for money, but it is a fact; and since it is a fact, and an indisputable fact, in my view, in all the countries I have ever visited, it proves persons to be in the wrong who say that as trade contracts and as prices fall, less money is needed by the nation, because the demand for money is falling. It is a fallacy. It is a fallacy based on the belief that the only demand for money is to effect current business; in other words, a medium of exchange demand.

In actual reality, you have a second type of demand, namely, the hoarding or store-of-value demand, which increases during slumps, and increases even faster than the medium of exchange demand falls. That is the most neglected feature of all discussions on money that I have ever listened to.

Having made that point, let me go to the question of solving the problem of adjusting the supply of money to these two joint demands.

The very essence of this—and of every other—trade cycle is that any initial decline in trade, when once begun, soon sets in motion a secondary lot of causes which are essentially "monetary," i e., (1) bank credit contraction, and (2) slow velocity in the turn-over of money—due to fear and/or the expectation of lower prices.

In other words, all cylical slumps when once begun, invariably assume, in their secondary phases, a monetary nature, i. e., a reduced supply of money, and an increased store-of-value demand.

Therefore, it is fallacious to argue that because [sic] the initial causes of the present slump were not monetary, monetary cures are not now appropriate. It is similar to a doctor arguing that a spectator who catches pneumonia at a football match should not be given oxygen because his disease was not caused initially by lack of oxygen.

What has happened in the recent slump is that there has been a 6-percent bank credit deflation—demand deposits—due to the member banks selling bonds faster than they have made new loans to industry; and a 15-percent decline in the velocity of bank deposits, due to fear of lower prices and worse trade.

And the slump will not end until the 6-percent bank credit deflation is "undone," and/or until the velocity of money is restimulated, either by threat of inflation or by a return of business confidence, perhaps originating from Washington. A few kind words might do the trick.

Now, a second rather difficult point in relation to the problem of money management:

Put briefly, there are two separate subdivisions of money management, and Mr. Goldsborough's bill, Mr. Chairman, I think you will agree, relates to a branch of money management, namely, the art of injecting an extra supply of money when considered necessary, and later of withdrawing it when it has done the desired work and shown signs of becoming dangerous in the opposite direction.

As I said, there are two separate subdivisions of money management. The first and least important consists of adjusting the supply of bank credit—that is, new loan money, to new demands—so that interest rates do not rise and industry is not hampered for lack of new banking facilities. The test of the success of this first subdivison of money management can be measured by the market rate of interest.

The second subdivision of money management, which is by far the most important from a national point of view, consists of keeping the total supply of deposits in existence—much of it, I admit, coming into existence by means of bank loans and investments—adjusted to the national demand for money—bank deposits—as a whole, so that commodity prices neither rise very rapidly nor fall very rapidly.

The test of the success of this second subdivision of money management can be measured by the state of trade, and the popular indices for commodity prices. For if trade gets worse, prices fall.

Mr. **Ford**. When discussing the injection of new money into the stream, can you tell us how this new money, this interbank currency that this bill provides, can be validated, in view of its not being complete legal tender; that is, in its being currency of a limited tender? It can only circulate among the banks; it has only one service use, and that is paying the actual taxes of the bank. Later on in the bill there is a provision for a change, but right at this point would you say that that was injecting new money when you are putting a limited tender into circulation?

Mr. **Angas**. Certainly. The interbank currency will inevitably give rise to a new normal type of deposit as it is born. The bank effecting the transaction creates a new deposit, which is backed 100 percent by the interbank currency deposit, so it is really the normal system working, although behind it there is an interbank currency note equal to 100 percent.

That is how I read the bill, although I do not appear as a supporter or condemner of the bill.

Mr. **Ford**. The Treasury just issues it.

Mr. **Patman**. What was that last statement?

Mr. **Angas**. I do not appear either as a supporter or a condemner of the bill. I do not presume to know enough about the technique of American ultimate administration of collecting these vouchers to give a dogmatic opinion as to whether the bill is practicable from an administration point of view. What I would venture to state is that from a general theoretical and practical point of view, the principles of its application seem to me to be sound, although there may be administrative difficulties which justify the bill not being passed; but, having visited numerous countries, I am fully aware that what can be put across in one country cannot be put across in all, and I would hesitate to express strong opinions about the administrative details of the vouchers in relation to this bill.

Mr. **Ford**. Well, Major, right there it seems to me that the crux of this bill is this interbank currency. The administrative details, as whether it will work, are a matter to be worked out on the basis of whether our sales tax will work, or something else, but in the operation of this bill we will assume that the difference between production and consumption is 20 percent. He sells $1,000 worth of some kind of an article. He puts $800, or whatever the amount is, in the bank, and gets credit for $1,000, and then the Treasury issues $200 of interbank currency to make up that balance, and that money is limited as to its effect to circulating between the banks, to be used for reserves on a 100-percent basis only. No fractional reserve loans can be made on it, but the bank can pay its actual bank taxes in that money.

The usual way of invalidating currency is to use it and give it legal tender for all purposes except taxes, but this gives it legal tender effect only for taxes. It is the reversal of the greenback idea, and I am just wondering if you have made a sufficient study of that to give us an argument that will validate that currency. You have made an analysis of the banking situation the world over, and there is very little difference between our system and the English system, so far as the validating of money is concerned.

Mr. ANGAS. I agree. It is only on that one circumference of the bill that I am afraid of the administrative side of it. I support the general philosophy of it.

Mr. FORD. We all do. But if you can bring up some plan that will balance production and consumption, we would be glad to vote for it, but there is the question of whether this interbank currency is that bridge, and whether or not that bridge has foundations under both its terminals, and those foundations are sufficient to support the weight that will go across it and ultimately make it a real passageway that will work all the time. That we do not know.

Mr. ANGAS. In my view, the bill will work admirably at the center of the circle. I have not studied the ultimate details of the technique at the circumference, the voucher system. I doubt at the moment if it will work, but I have not had time to question the author of the bill or anybody else. I do not think that you will be able, if this bill is passed, to differentiate between these reserves consisting of interbank currency notes and other reserves. I think that that would have to be cut out of the bill, for this reason, that if a retailer has collected vouchers, say, a million dollars, and goes with them to his bank, the bank will credit him, I presume, with a million dollars. That virtually happens in the end.

Am I right?

Mr. GOLDSBOROUGH. How is that?

Mr. FORD. $1,200,000.

Mr. GOLDSBOROUGH. What is the question? My mind was wandering.

Mr. ANGAS. If a retailer gets a deposit equivalent to the new interbank currency notes of, say, a million dollars in his bank, he may want cash of $1,000,000, and what will happen to the banker? If cash for a million dollars leaves his bank in the form of ordinary notes, Treasury notes, Federal Reserve notes, and all that, the banker will have to contract outstanding credits, assuming that he has no excess reserves, equal to whatever the ratio is at the time, three to one, or whatever it is, on the 20 percent reserve ratio backing, with the result that that banker might have to contract three times as much outstanding bank loans to other people so as to keep his ratios correct, because the interbank currency only backs an equivalent amount of bank deposits, and when those bank deposits be cashed for noninterbank currency notes, the squeeze begins.

I am sorry that I expressed that so badly, but I can put it in writing better.

Mr. GOLDSBOROUGH. Major, maybe I can be of assistance to you right there. I do not know how carefully you read the plan provided for in the bill, but the bill is so written to enable the banks, insofar as their ordinary business is concerned, to transact it exactly as they formerly did. There is a separate department of the bank for this credit which we call interbank currency. That credit constitutes a deposit which the bank can loan, but it can only loan it once. The fractional reserve of that bank remains intact. It does exactly what it always has done.

Mr. ANGAS. Yes; I appreciate that, sir, fully, but there is a fallacy in it, in my view. I am not prepared today to analyze that fallacy. I was going to do that later, if I was asked to, when we came——

Mr. GOLDSBOROUGH. If you can look into that between now and tomorrow——

Mr. ANGAS. If you wish me to come again, I will come prepared to answer that technical banking question. I am sure I am right, and you are sure you are right——

Mr. GOLDSBOROUGH. I am going to ask you to look into that between now and the next time you appear, which we hope will be tomorrow, if you can stay over.

Mr. ANGAS. I will, with pleasure, sir.

Mr. PATMAN. May I ask that he consider the fact that in this bill all retail stores will have to be licensed, and anyone can be licensed under the act, and that anyone obtaining a license can have the privilege of receiving these 15 percent or 20 percent discounts from the bank, and I would like to have the Major's opinion on whether or not that would open up the floodgates for graft and corruption, and I understand that it will probably destroy our whole monetary system, but I would like to have his views on that.

Mr. ANGAS. Yes; there would be a tendency that way.

Mr. FORD. Pursuing my question just a little further, you know that this bill provides that there may be a call on the bank for currency. Assuming that a customer went to the bank and said, coming back to the million-dollar example that was referred to, "I have to have $1,000,000 in currency right away", and the bank gives it to him. That depletes the funds of the bank, and this bill provides that the bank can send its interbank currency to the Treasury and have the Treasury issue $1,000,000 worth of some kind of notes of the kind that the bank gave to this man, real money.

I have suggested that possibly a way to cure that situation would be, later on, when things straighten out, to have the bank ultimately send back to the Treasury regular currency and get interbank currency in its place, so that the interbank currency would always be a cushion to be used in its reserves on a 100-percent basis.

What I am trying to get at, and what I think every member of the committee would like to know, and what we hope somebody in the course of this hearing will clear up, is how we will validate that interbank currency as real money.

Mr. ANGAS. The banks can cheat. I do not see——

Mr. GOLDSBOROUGH. I am going to suggest, with your permission, that I think you are just as wrong as you can be today, and I am going to suggest that you do not go into that, if you will permit me, until you have read the testimony.

Mr. ANGAS. I would much prefer to do that, because I have not read your evidence. I have read all of the other evidence except yours, and I was going to do that tonight.

Mr. FORD. I cannot see how the testimony will alter the facts respecting the bill.

Mr. ANGAS. I agree that the provision in the bill which enables interbank currency to be cashed at the Treasury will supply the bank with cash equal to the deposits, but how is the Treasury to know whether a public demand for cash is a true one, or whether it is a little trick on the part of the bank so as to increase its excess reserves? How?

Mr. **Goldsborough**. It could not be used to increase its excess reserves, and that is the reason I suggested that you answer that later. It can only be used to pay over the counter if there is a run on the bank, if the bank needs cash. That was all gone into in the previous hearings.

Mr. **Angas**. I may have missed the point entirely, but I feel that there is a snag, and I would like to leave it, as you suggest, until later.

Mr. **Patman**. Another point for consideration I wish you would consider in connection with the bill before you is that the bill provides that the discount will only be given to individuals. It will not be given to corporations. There are $40,000,000,000 of retail sales a year, or there was last year. Of course, a like amount of that was to corporations, and it just occurred to me that it would be almost impossible to administer a law like that, it view of the fact that if you wanted to buy something for a corportion, you would buy it as an individual and then sell it to the corporation. As an individual, you would be getting a 15 percent discount.

Mr. **Angas**. The same thing occurred to me, sir.

Mr. **Patman**. If you bought an ordinary automobile for $1,000, you could turn around and sell it to a second-hand dealer and get the 15 percent discount, and another dealer could sell it and get the 15 percent discount, and everybody could get rich.

Mr. **Angas**. I see the point, and the same administrative difficulty occurred to me.

Mr. **Patman**. But somebody will have to pay the bill, and what I want to know is, who will pay it?

Mr. **Angas**. I find a difficulty in defining "retail trade" with a clear-cut edge, or in defining an ultimate consumer. That is why I am doubtful about the administrative features, and why I wanted to discuss later the circumference problems of the bill as distinct from the central problem.

Mr. **Patman**. Another thing, Major. If a farmer gets a license to sell eggs, there is nothing to keep him from selling automobiles at the same time, and you would soon have 10 or 15 million retail dealers in this country, instead of one million and a half, and everybody would be selling to one another and getting the 15 percent discount.

Mr. **Angas**. I think I agree. In fact, I have been encouraged in trying to invent means of making money out of the bill, because that is an ideal way to approach the wisdom of a bill, but there again I would prefer, as the Chairman suggests, to study that before committing myself to rather snap judgments on the American administration of it, I not being familiar with the details of American administration.

Mr. **Ford**. Would that bill work in England?

Mr. **Angas**. I have not yet had time to go through the administrative problems on the circumference, to give an opinion, sir. You must forgive me, but I am without notes or without preparation on that.

Mr. **Ford**. Maybe that was not a fair question. Under the English banking system——

Mr. **Angas.** May I interpose? I think it would be more difficult in England than here.

Mr. **Ford.** But under the British banking system, assuming that this bill were put into effect, if the British retailers went to the Midland group and turned in their $800 each time they sold $1,000 worth of goods, and the Midland Bank gave them credit for the $1,000, where would the Midland Bank get its deficiency from?

Mr. **Angas.** It would not get it.

Mr. **Goldsborough.** You are going to get yourself in a hole. You had better read the bill before you testify on that.

Mr. **Angas.** Thank you for rescuing me. You might have all sorts of sources, the Bank of England, or you might invent another one. I do not presume——

Mr. **Ford.** To clear my mind on the relation of the banking system in England to British trade, the Bank of England is a private institution, and its policies are largely dominated by the Exchequer.

Mr. **Angas.** The Chancellor of the Exchequer.

Mr. **Ford.** He practically dictates the policy, does he not, as far as it affects British trade, and all the rest?

Mr. **Angas.** The Treasury officials, really.

Mr. **Ford.** And the British Treasury itself, I presume, comes to the rescue of the Bank of England at times? Isn't that true?

Mr. **Angas.** Undoubtedly.

Mr. **Ford.** Then there are times when the Bank of England comes to the rescue of the British Treasury?

Mr. **Angas.** Undoubtedly.

Mr. **Ford.** So there is a working agreement there?

Mr. **Angas.** Called a gentleman's agreement.

Mr. **Ford.** Now, we have in this country what is known as the Federal Reserve, the function of which I am assuming you are familiar with. The Federal Reserve does not in effect come to the rescue of the Treasury any more than as a vehicle or a tool through which the Treasury performs certain functions. The relationship is not parallel at all, is it? They are not identical?

Mr. **Angas.** They are not identical, but similar in tendency.

Mr. **Ford.** Similar, but not identical?

Mr. **Angas.** Yes.

Mr. **Ford.** The thing that we are talking about here is that the Treasury of the United States—and here is the point that has not been developed to any great extent, but I think it will be later, that the production of goods in the United States is a national problem, the keeping of the production up to that medium of exchange in the hands of the people that will consume that production.

Now, then, here is a retail volume, we will say, of 40 billion dollars. Of that amount you have given the retailer a discount of 15 percent or 20 percent. That would be 8 billion dollars in the way of a deficit, over the amount actually placed in the bank by the retailer. Then the Treasury of the United States steps in and says that the banks of the country have in their vaults 40 billion dollars worth of credit, but there is that 8 billion-dollar deficit by reason of the fact that they have given a 20-percent discount to the retailers.

Mr. **Angas.** When you say "deficit," do you mean a Budget deficit?

Mr. **Ford.** Not in that sense. There is a distinction there.

So the Treasury says, "All right; we will issue 8 billion dollars' worth of Treasury interbank currency against the amount that the banks have given the retailers credit for, and that transaction stands even at that point. But these banks, having this 8 billion dollars' worth of interbank currency, are suddenly called upon for a large amount of cash, and by reason of the intermediate currency volume in there, they do not have it, so they send that 8 billion dollars of interbank currency to the Treasury and get 8 billion dollars of actual Treasury money and they use that money to pay their depositors.

That goes on for, we will say, a month or 6 weeks or 2 months, and the demand has been supplied. The deposits begin to come back into the banks, and the banks assume their normal functions, and they find that they still owe the Treasury for that interbank currency, so they begin to send back real money to the Treasury and get back for that money interbank currency, to balance it up.

Possibly that will work. I do not know, but I would like to have somebody who has made a very intensive and close study of monetary relations between treasuries and banks, tell me whether or not in his judgment that interbank currency, based on the productive capacity of the United States and the ability of the people to consume that capacity, constitutes a warranted draft.

Mr. ANGAS. What is the adjective before "draft"?

Mr. FORD. Warranted. Think about that, because it is the crux of this bill.

Mr. ANGAS. The answer to that hangs on my further study of the evidence of the constructor of the bill. The draft is warranted insofar as you want to increase consumption.

Mr. LUCE. May I ask if the Major has completed his general statement?

Mr. ANGAS. From my point of view, no, sir; but if it wearies you, I will stop. I would like to develop a few points further, if the Chair thinks it suitable.

Mr. GOLDSBOROUGH. I will say, Mr. Luce, that Major Angas was very anxious, he told me this morning and also yesterday, to complete his statement. He said that he would study the testimony and the details of the bill, and when he had completed his general statement, he would then analyze and discuss the bill in detail. That is the reason why I suggested that he proceed without interruption, but, of course, the committee should use their own judgment about how they want to question a witness. I think that he would prefer to proceed and complete bis statement.

Is that correct?

Mr. ANGAS. I do not presume to make suggestions, but I would personally like to finish my case, which will soon be ended.

Mr. GOLDSBOROUGH. There is no hurry, sir.

Mr. MCKEOUGH. May I interpose for just a second?

Mr. GOLDSBOROUGH. Yes.

Mr. MCKEOUGH. I take it, Major, that you have been developing your case in connection with the philosophy outlined in your bulletin, or digest No. 14, except for the interruptions that have been interposed? Is that your program?

Mr. ANGAS. Yes, very briefly. I was going to touch on that, because it is the key to the capitalistic system.

Mr. MCKEOUGH. May I suggest that he proceed to that conclusion, because it is in connection with that that I would like to ask a few questions.

Mr. GOLDSBOROUGH. You mean for him to proceed?

Mr. McKEOUGH. With his statement, so that he can develop his theory on the causes of slumps.

Mr. ANGAS. Shall I proceed, sir?

Mr. GOLDSBOROUGH. Yes.

Mr. ANGAS. To continue in relation to the present slump, it was in my view caused very largely for monetary reasons, because the total quantity of money was accidentally deflated 6 percent in the last year, and because monetary velocity declined. The slump itself meanwhile has not been cured, because the accidental deflation has not yet been undone, nor has the decline in velocity demand and business fear been counteracted.

The reason why I venture to call the deflation of bank deposits accidental is because the Chairman of the Board of Governors of the Federal Reserve System stated in an article in Fortune, in April 1937, that he personally did not think that prices had risen sufficiently to justify a deliberate contraction of the supply of the bank credit. The actual contraction occurred, from the point of view of the Chairman of the Board, accidentally, because the member banks became nervous about the future rate of interest and sold their own bonds in anticipation of a coming slump in bonds, and an additional reason for the member banks selling bonds last winter was that, on the tightening up of reserve ratios by the Board of Governors, the out-of-town banks called their New York and Chicago balances away into the country, which somewhat strained the reserve ratios, particularly of the New York banks, so that they, for a second reason did some selling, particularly of longs, and it was those two factors which accidentally, from the point of view of the article in Fortune to which I refer, caused the 6 percent deflation of the effective national supply of bank-credit money.

In my view, it was certainly correct to stop the generally wild price boom in March by monetary measures, and by the weapon of talk, for then the disease of boom prices was monetary, as proved, in my view, by the fact that almost all prices and wages were rising, as distinct from only a few monopoly prices. It was in fact the value of money that was then depreciating and causing the bear market in money itself and the bull market in commodities. The deposit inflation of 1933 and 1936 had in fact caught, and I might add that the casual fortuitous factor of expected war, leading men to anticipate a shortage of materials, led to speculation in materials and borrowing of bank moneys to buy materials to hold for the rise and the expectation of rising prices, simultaneously stimulating the general velocity of money, at all events, for a measure, too, although it is difficult to prove that assertion by statistics.

So much for checking the wild boom that was developed last March, which was due not to monopoly prices, in my view, but to the catching of the inflation.

As regards the subsequent slump, it was caused not by monopoly, nor, in my view, by lack of balance in price structures, and in wage structures, but by a deflation of money due to the banks selling bonds and a deflation of velocity demand and fear of certain Government policies, of certain labor happenings at that period, and a decline in velocity was further stimulated by the businessman's memory of 1929, and also the investor's memory of 1929, a most important factor in this recent mystery slump. In any slump or in any boom, the businessmen and the investors always remember what happened to them in the last business slump or boom, and they become particularly cautious and make attempts not to be caught with the same business or investing errors that they committed in the last previous boom or slump. They usually remember the last boom or slump, and partially forget the penultimate boom and slump, and almost totally forget the previous ones, with this economic result, that no trade cycle is similar to the previous one, and rarely similar to the one preceding that, although perhaps it is more similar to the cycles in the more distant past, and that is because men as a whole learn from their mistakes.

Well, the last slump was caused not by monopoly, as it is the fashion to say, but by deflation of bank credit and deflation of velocity; and such deflationary slumps, especially when there is clearly not enough monopoly to keep the general price level up as distinct from a few prices, can I think certainly be countered by scientific inflation, or, if you prefer a drawing room expression, reflation, according to the accepted principles of managed money, of increasing the supply of money when the real price of money rises and general prices fall, but that was not done. There has been a 35 percent fall in the Moody Index of sensitive commodities, and a 12 percent, if not a 15 percent, fall in general commodity prices as measured by less sensitive indexes, and there is now going on a fall in wages, or the price of labor, coupled with a 10 percent fall in bonds, or more, and a 50 percent in stocks. There is in fact a bull market in money.

Now, as regards cures to trade slumps, millions of people produce millions of different schemes to create a better world, and under certain conditions, most of these schemes are panaceas which might prove effective under certain conditions, but the condition that we are concerned with is the modern capitalistic system, and it is a fact that most curative schemes to the trade cycle coming both from politicians and professional economists, and social reformers, neglect the realities of present-day life. They forget the true nature of capitalism and of the profit system. Whether we like it or not, we have a profit system, and no scheme of eliminating the trade cycle which does not take account of the profit system can have success, and that applies to monetary panaceas, as well as panaceas based on the redistribution of wealth, or even the totalitarian state, so long as some profit-making companies exist.

It is correctly said that under the capitalist system profits are the mainspring of prosperity and employment.

Under capitalism it is the employers who give employment and incomes to workers; and in self-defense they will cease to do so if they do not foresee a good chance of profit. Business profits, it is true, are usually only about 7 percent to 10 percent of the total national income, but profits constitute the 7-inch tail which wags the 93-inch dog of prosperity.

All workers know this thoroughly; they know that profits are the key to their jobs.

The Government therefore, so long as the capitalist system endures, must, in order to insure full employment and decent wages for workers, first aim at securing good profits for business.

Similarly, trade unions, if they wish for continuously high wages, or for higher wages, must make certain that business men make high profits first; for it is only when profits are ample, or are rising, that business men can be induced to employ more people or to pay out higher wages. Indeed, as soon as profits disappear, production, employment, and wages are all lowered.

In other words, the way to cure a slump in employment is to aim at raising business profits.

This statement, although true, is however politically unpopular; and it seems to irritate kind-hearted people—for it seems to them to imply an "unfair" policy of enriching the rich, before enriching the poor.

But in actual practice, as long as capitalism endures, the profit factor is a fact which has got to be reckoned with, and the fostering of profits is the policy that governments should primarily pursue—even in democracies where the statesmen in office are rightly and chiefly concerned with the underprivileged third.

What then is the nature of the profits, upon which prosperity so greatly depends?

Profits, obviously, are the difference between costs and prices.

As regards costs: Manufacturing costs are comprised of wages, materials, and fixed charges. And they must be covered by prices, in order to give profits.

A great many costs, however, are fixed by legal contract; or are, at all events, comparatively rigid—for instance, debt charges, rents, local taxes, mortgages, and a good many other overheads and contractual salaries.

These so-called contractual rigidities make movements in the general price level highly important, under modern capitalistic economy. Let me explain.

Obviously, if the general price level of commodities is, say, cut in half, while all the fixed charges of business remain stationary, twice as many goods will have to be sold by producers in order to satisfy their fixed charges; with the result that, unless twice as much trade is done, money profits will rapidly diminish, and confidence will be upset.

On the other hand, if the price level is doubled, instead of halved, only half as many goods will have to be sold to satisfy fixed money charges, and the resultant saving is all profit to the employer—a condition which will soon enable wage earners, with the help of their unions, to extract a larger share for themselves.

It is, of course, impossible to state, with absolute precision, what the general price level, as measured by index numbers, should be in America today. But it is quite certain that a sudden 50 percent fall in general prices would eliminate most profits, owing to the fixed debt level and the other contractual rigidities; and thus further aggravate the present depression.

Errors, in the general price level, in relation to the debt level, can however occur on the up side as well as on the down side.

For instance, a sudden 100-percent rise in the general price level would be unfair to creditors, pensioners, and all other persons with fixed incomes; and incidentally would soon set in motion an unhealthy condition of disequilibrium in consumption. Indeed, if prices doubled, people with fixed incomes would only be able to buy half as much as formerly, and there would thus be considerable dislocation in the consumer goods industries—in addition to the whole process being most unfair to creditors.

Now, in a situation where profits disappear, trade stops, confidence diminishes, and trade stops further. Therefore, under the capitalist system, one must find a method of reflating profits, and in order to do that you can do two things: you can lower wages, or raise prices.

As regards the normal custom, or natural custom, of attempting to lower wages, which is an inevitable policy for businessmen to pursue if there is no effective money management such as would raise prices again, if you agree that businessmen cannot continuously run into loss, then they must try to reduce their costs so as to restore some profit and to prevent all of their working capital and cash balances disappearing. You will agree that the businessman can do virtually nothing about his fixed charges. They are the rigidities. You will also agree that he has no personal control over the price of his raw materials. It therefore follows that the only thing left for him to do is to attempt to cut money wages.

In respect of the policy of cutting money wages, it is often argued that the policy is economically harmful to the Nation as a whole, because it reduces purchasing power. There is some truth in that contention, but it is largely a fallacy, for the policy of reducing wages is one of redistributing the national income, however big or however low, more in favor of the profitor, at the expense of the wage earner. Indeed, other things being equal, if you permit that dangerous phrase, a cutting of wages which benefits the employer enables an employer to spend money which otherwise might have been spent by the wage earners with their higher wages. It is a redistribution of the proceeds of the continuous process of sales, rather than the elimination. Indeed, if you cut wages 50 percent, you might raise profits by a large amount, so that dividends might rise by mathematically about the same sum of money that the wages were cut. But under capitalism, you have to do something which restores profits.

Now, we all know that an attempt to cut wages is unpopular with wage earners, so let us look at the alternative method, of reflating profits in a period of bad trade. But, just briefly, before doing that, let me mention that business men invariably not only try to cut wages, but also try to prevent prices falling further by reducing production. Shortly I am going to talk about getting prices up, but businessmen in a falling trade market cut production in the hope at all events, of stabilizing prices by reducing total output, and this is one of the ludicrous features of the capitalism under which we live.

In order to revive trade and make the Nation richer, we pursue a policy of reducing the output of goods, which makes the Nation poorer in real things than it otherwise need have been, and that is why I said yesterday that a few intelligent people getting together and debating this problem—I do not say for weeks, maybe for months on end—ultimately should find the invention which will remove this anomaly, not only of plenty, causing poverty and want, but also of trying to make trade better by reducing the world's wealth deliberately It is a foolishness, and that foolishness in the course of time can be made to disappear by thought.

The businessman cannot help cutting production. That is just self-defense. He cannot afford to go on producing full outputs at a loss. Certainly the businessmen of the country as a whole cannot do so. I know that it is customary to point to Mr. Ford's behavior, with his automobiles—was it the T model?—where he sold 400,000 cars at a loss in order to stimulate demand eventually, but what is true of a single company is not necessarily or even usually true of the industry as a whole. I won't go into the rather complex mathematics of that, unless I am pressed to. But why a businessman cuts output is partly not to make further losses himself and partly to stabilize the price of the product, or, if it is, to get the price up again.

Look at all the restriction schemes of the world today—tin, copper, oil, cotton, wheat, diamonds—everything, almost, prices governed by scarcity, a sad policy, but an inevitable one; nobody's fault, resting on the apparent necessity of reducing the output of the goods so as to get prices up rather than increasing the supply of money so as to get prices and profits up, and if there is no central monetary authority, or group of money managers, who are not only given the job of getting prices up and of preventing their fall, but also to act in such a way as to see that it is done in practice, and if the money managers are either not there or do not fulfill their economic function, the businessman must in self-defense, in order not to become bankrupt, reduce production and try to lower money wages.

Mr. TRANSUE. Do you include the farmers in that category of businessmen?

Mr. ANGAS. Yes, sir; all businessmen of every character.

Just a last sentence, and it is over.

The implication of what I have said is that a monetary manipulation so as to send prices up again, no matter what the cause or the fault, is desirable even when the manipulation is only temporary. I know that it is customary to say that you cannot increase the wealth of a country by increasing the bits of paper. I know it is customary to say that such a policy is ludicrous, but that contention appears to me itself ludicrous, because we live in a price economy, and business men seeking profits seek them in terms of money, and the profits in terms of money come from the price level, and, courageously altering the supply of money or bits of paper is a factor which restores the price level, and then restores the production of wealth and the consumption of wealth, so that what we term the trick—I do not object to the word—the trick of manipulating money and creating bits of paper, or ledger entries in bank books, out of nothing, can increase the supply of wealth as a secondary result.

That, sir, is my case for managed money.

Now, on this matter of political money management, I agree that rising prices lower real wages, and if the worker again, and the people who derive incomes from fixed overhead charges, are getting so much of the sale price of a product, that the profitor gets none, you must have a redistribution of the wealth in favor of the profitor to get the system running again, which implies that the wage earners suffer lower money wages, lower real wages, or reduced employment. Wealth has to be distributed in favor of the profitor.

The beauty of the reflating process, of reflating profits, is that the wage earner does not bear the whole burden, but that it is partly shifted to the creditor class, or the people who derive incomes from fixed overhead charges, so that the burden of reflating profits is shared—the reflating process is shared. The amount that they have knocked off of their net total is relatively small, but a small change in real wages, or in the real reward of the fixed income group, means a much higher percentage change in profits. It is that little bit of redistribution in favor of the profitor which gets the system working again, and it is just a little bit too much in wages or a little bit of a fall in general prices which give real rewards to the other factors of industry at the expense of the profitor. You do not need big changes.

Mr. GOLDSBOROUGH. You see, Major, in making that argument, your are confronted with history. History teaches us that labor has never had any of the normal comforts and luxuries which make life worth living, so that I do not believe you mean by that argument that the lowering of wages tends to general prosperity, do you?

Mr. ANGAS. Yes, sir. As the French say, going back a little so as to get the thing spinning again, repriming the industrial pump can to some extent be done by lowering wages. I do not like to say it, but I believe it is so.

Mr. FORD. Might I ask this question, to see if I get your slant correctly? Do you advocate reducing the price of goods and services, so that redistribution will be more widespread, or do you advocate the increasing of the money supply to meet that volume of goods and services?

Mr. ANGAS. Increasing the money supply, sir.

Mr. FORD. So that the goods will be distributed at a profit?

Mr. ANGAS. So as to get a profit, yes; so as to reflate profits, the key on which the whole thing hinges in capitalism.

Mr. TRANSUE. Would you say that the profits of corporations this past year have not been enough in the United States?

Mr. ANGAS. They were ample in the first few months, but in the last 3 months they were not ample.

Mr. TRANSUE. I read an article in the New York Times last Sunday, and I think one on the Sunday before, showing that the profits of corporations, even taking into consideration the labor difficulties in the early part of the year, and the slackening in the latter quarter, were very substantial.

Mr. ANGAS. Yes, sir.

Mr. TRANSUE. What is the answer, according to your theory? That those must be increased?

Mr. ANGAS. From the present level, yes; particularly as the anticipation is that they will fall.

Mr. TRANSUE. Another thing along that line is that in the State of Michigan they have a sales tax of 3 percent. That sales tax showed that the retail business was higher, during 1937, up until about the middle of November, than it had been, that there had been an increase month by month over the prior year.

Now, would not that indicate that as far as the consumption of consumers' goods is concerned in the State of Michigan, it was going along at an increasing rate, together with the corporation profits? I do not know about the country as a whole.

But just what caused this stoppage of trade and work, and the lay-off, for instance, of 30,000 men in the General Motors industry all of a sudden? That is the thing that I am interested in.

Mr. ANGUS. Yes; it is rather surprising, in view of the fear among businessmen, how in certain sectors of the country the retail trade has kept up. It always does keep up, partly because retail distributors tend to raise prices at the tail end of a boom, because they have placed orders at the higher prices, and, with the usual 30 percent mark-up, or whatever it is, you get a higher price, which, even with a smaller volume, tends to show a greater statistical amount of trade in terms of value.

The other reason is that people, during waves of prosperity, get into the habit of spending more, particularly their wives, and they make many commitments to do things in advance, like furnishing a house, and they will even go on buying quite heavily after the beginning of a slump is apparent, because they have the picture rolls to put up, or the carpets or linoleum to lay down. I think that that is why there is a lag in the retail trade slump, and another reason is that a great many dividends are not cut until perhaps 6 months after the slump begins, so that people who are eventually going to suffer do not suffer immediately, but I agree myself to a state of bewilderment at some of the statistics which appear, particularly around Michigan.

Mr. TRANSUE. There is a further reason, it seems to me, and I wondered if you have considered it, that in the production of automobiles, which is the principal business of some of the cities of Michigan, there is the selling on installment, the easing of sales. Has that contributed anything to the situation?

Mr. FORD. It has to the used-car market.

Mr. ANGAS. I think that the installment system is a bogey which one need not fear as much as most people think. But to try to prove that case will take at least 10 minutes. I do not attribute the slump to the so-called buying in advance of income, for this reason, briefly, that if I buy something on installment, and the purchase is mainly financed by the seller, who borrows from a bank, the middleman from whom I get, say, a refrigerator enjoys a decline in inventory, and unless he has suddenly changed his inventory policy, he gives a replacement order to, let us say, the Kelvinator Co., with the result that the Kelvinator Co. pays, while reproducing another refrigerator, a sum of money to the general public, roughly equaling the amount that I have spent in advance of my future anticipated income, so that somebody else's income in some other part of the country goes up mathematically by about the same amount as I have pledged my future income, and if you multiply me by 130,000,000, it is a pretty good guess that my income will go up more than I anticipated. In other words, the national income from reproducing goods bought on installment rises at about the same value as the installment pledge, so that incomes pledged for the future mature almost immediately in the present, unless the inventory policy of the middle man has changed, and that is the big snag.

Mr. TRANSUE. Following that a step further, there is a saturation point for refrigerators or automobiles at a given price under the present installment system of selling.

Mr. ANGAS. Yes; that is true, and money management will never solve the problem of saturation. There are a lot of problems that it won't solve as regards single industries. In all countries the demand for pepper, salt, and mustard is easily saturated. In this country the demand for cars is probably pretty well saturated; in my country, fairly well; in Germany, hardly at all. It is true that some industries can produce up to the mental saturation point of the population, and then they have their slumps, but all industries cannot do so, because there are comparatively few commodities in the world or in a country for which there is not a mental demand, and although one class, one income bracket—we will say the fourth from the top—may have bought all that it requires of a thing, say, mink coats, there is always something else above, like a yacht, in the other bracket, which it would like to buy if it had the money, so that although the demand for mink from that income group may disappear or become saturated, there is almost certain an income bracket just below, we will say the fifth from the top, with a mental demand for minks.

So that one may talk about a few things becoming saturated, like the demand for spectacles, all in one instant, but generally it is not true.

Mr. **Transue.** Just one more question, and that is this, as to the effect of technological improvements upon industry as affecting the number of people out of work. That comes into this problem a great deal, too.

Mr. **Angas.** Money management helps there, I think.

Mr. **Transue.** In other words, in a mass-production industry.

Mr. **Angas.** You will appreciate that you are asking me a question which no economist has succeeded in discussing at all well in less than 20 pages.

Mr. **Transue.** It is something that we have to take into consideration—isn't that true?

Mr. **Angas.** Yes; it is true. Briefly, I admit that technology can discharge men, and they probably have to lower their wages asked, so as to get a job quickly. Much unemployment is due to wages asked being too high to attract a buyer. Technology, I admit, creates unemployment, and it tends to lower the wages of the men who are unemployed; but remember this, that technology of this nature usually means not only a fall in the costs of the thing produced, but a fall in the final price, so that, to round it up, people who might have paid the higher price before there was technology now pay a lower price and have more money left over to compete for the unemployed men, but this subject is very involved.

Mr. **Transue.** It is, but I am wondering whether or not you have examined the materials, the goods produced at mass production, and whether or not the improved technology has given a decrease in price of the article to correspond with the improved article.

Mr. **Angas.** Sometimes yes; sometimes no. It depends on the state of competition, largely, and on the sales policy of the firms who put it into effect.

Mr. **Transue.** And the number of firms in that particular industry has something to do with that, too.

Mr. **Angas.** That factor enters into my statement on the state of competition, yes.

Mr. **Transue.** In your view, does that situation affect our present condition in this country?

Mr. **Angas.** Very little. Changes in technology for the country as a whole are rather slow.

Mr. **Transue.** Here is a question that I asked sometime ago and did not get an answer to—not from you, but from another witness who appeared before this committee.

Generally speaking, when there is no longer a market for the products of manufacturers in mass production at a given price, they lay off men. In agriculture when there is no longer a market at a given price, prices fall and production keeps on at the same level.

Are these factors in our economy that must be brought into balance, in order to have prosperity?

Mr. ANGAS. It is desirable. I do not think that money management will entirely solve the surplus agricultural problem, but it will tend to take up the slack of unemployed men, thereby increasing the demand for agricultural products. In some branches of agriculture, like rubber, you invariably find that when prices fall the native laborer produces more instead of restricting, like producers under capitalism do. He says that he must get more rubber from the trees so as to get the income that he requires from a larger volume, so that they overproduce egregiously.

Mr. FORD. Speaking of technology, Major.

Mr. TRANSUE. Let me follow that one step further.

You spoke of fixed charges as far as business was concerned. Agriculture has fixed charges in connection with the interest on mortgages, and taxes.

Mr. ANGAS. Very.

Mr. TRANSUE. So that the farmer is not only up against the same proposition, that he has to produce more on a falling market, but he has the same fixed charges on his mortgages and the same taxes to pay.

Mr. ANGAS. I think that the individual, uncontrolled farmer will try to produce more even in crops like wheat, which takes a few months to grow. Rubber you can tap at any time. So that case of overproducing aggravates the general situation in the case of the individual man, and that, I believe, is part of the philosophy behind the new farm bill, but I am not an expert on it.

Mr. FORD. Major, you were talking about technology. Our advertising used to carry the advertisement of the Fisher body, and they still carry it; and originally in connection with the manufacture of automobiles the Fisher body meant something. They had trained mechanics, experts in their line, and they produced a thing of beauty and a joy forever. But the same concern today, instead of having 10 men work on that body to produce it, will put it under a great big stamping machine and bring it all out in one smash, and all that they have to do is to trim it up a little and polish it and paint it, and therefore there should be less men employed on the automobile by reason of the mechanical method of producing those bodies. As an actual fact, there are more men employed in building automobiles today than there ever was. The reason is that they are able to produce that machine today for $900 that in the old day would have cost $2,000.

Mr. TRANSUE. You said that there were more men producing automobiles today.

Mr. FORD. I mean generally. I am not speaking of this particular day, but I am talking about generally. About 3 months ago there were more men producing that volume of automobiles than at any time in the history of the industry.

Mr. GOLDSBOROUGH. They were producing more automobiles then.

Mr. FORD. Yes, and there were more men producing them. So technology did to that extent contribute not to the cutting down of the number of men, but to the increasing of the number of men.

Mr. REILLY. Where do you get that information?

Mr. FORD. I read it in the papers.

Mr. **Reilly**. I challenge it. I think you will find that in the steel business today production is increasing and the number of men decreasing.

Mr. **Ford**. There were 298,000 men employed in the steel industry in the middle of 1937, who were producing a great volume of steel. In 1929 there were less than 250,000 men in the steel industry, when we were producing also a great volume of steel.

Mr. **Transue**. Here is something to take into consideration in that, that the number of hours worked every day, and the number of days worked per week, and the number of days worked a year should be taken into consideration. In other words, have you the statistics along that line?

Mr. **Ford**. About 4 years ago they were working about 12 hours a day, in two shifts. Today they are working 8 hours a day in three shifts.

Mr. **McKeough**. That accounts for the increase in the number of operators.

Mr. **Transue**. But are they working three shifts?

Mr. **Ford**. Not right now. It is down to about 28 percent.

Mr. **McKeough**. Of production.

Mr. **Ford**. But they were up to 84 before, but I am talking about the peak load.

Mr. **Transue**. You are talking about when they were working as fast as they could.

Mr. **Ford**. But technology is not the reason for their not working now.

Mr. **Angas**. Much depends on the so-called demand elasticity for the product of the particular industry when technocracy is occurring. In motorcars, in an unsaturated country, you have a highly elastic demand for steel. I do not think the price of steel affects the demand very much, except for export, and technocracies occurring in the steel industry will probably leave the men unemployed much longer in that particular industry than it will in automobiles, for which the demand is fairly elastic, but money management won't solve the problems of single industries except insofar as it eliminates the general slump.

I favor the capitalist system, with well-managed money. I believe in the rough brutality of profits. I think they create cheapness. There are members of government who object to profits as such being temporarily high, because they are regarded as exploitation and, for those in steel, or cement, there may be the argument that it delays the building revival. I do not much mind if profits are temporarily high, provided that there is no monopoly, because when the profits are temporarily high, new capital flows into the industry, leading to an augmentation of plant and eventually to an increased supply and more intense production and a cut in prices, so that the consumer gets the ultimate benefit in low prices, and profits largely disappear and become low again.

That is the rough process of capitalism in a single industry, and I cannot imagine a State intelligent enough to take control of all industries and regulate the thing itself.

Mr. **McKeough**. May I ask right there, following your theory of profit as the mainspring, this: I understand your philosophy to be that it is primarily based on enlarged profit during a slump period in order to create greater activity industrially?

Mr. ANGAS. Yes.

Mr. McKEOUGH. Following that further, whenever profits are higher, obviously, then, if your philosophy is sound, there should be no disturbance, assuming that the profits continue to enlarge.

Going back to 1921 and 1929, and taking big steel's earnings, there was approximately $6 a share earned in 1921 on the common, and that was raised to $21 a share in 1929, so that, if your philosophy is the answer, and it is purely on the profit side and the capital invested in the industry, those that offered the philosophy of the new era in 1928 and 1929 were apparently justified by your very interesting presentation of your philosophy here today, when they thought that they must be entering a new era, when they rather aptly sloganed the idea of two chickens in every pot and three automobiles in every workman's garage, which was to be the answer—

Mr. TRANSUE. Two of them, as far as the automobiles are concerned.

Mr. McKEOUGH. I will enlarge on it, and make it three.

What I cannot reconcile is, if that is the program, in our attempt to bring about the solution of these vicious upswings, and downswings in industrial activity, with resultant depression and prosperity, what happened in 1929, with the profit reflected throughout the industry, which was so largely participated in by big steel? May I anticipate your answer by saying, because I understood your presentation, that it was the strained credit development that came about, that somewhere along the line there was someone or some group that anticipated that things were not as they seemed, and I presume there may have been an exception in your case—I do not know, but, generally speaking, every acknowledged economist, every so-called prudent banker—and I do not want to become facetious, but you used the words "prudent banker" many times in your presentation, and I wonder if they merited it by reason of the performance of 1921 to 1929, 1931 and 1932, 1933 to 1936, and from 1936 on? I sometimes wonder if they should have that high compliment that the word "prudent" implies. But we were in that picture, and something happened.

Now, I am wondering if there has not been some cause for the effect. There always is. What is that cause? Who is it that give that word out that things are not so good, call your loans, freeze up on advancing any further loans. It is not the Government of the United States, because there is a rigidity as to the ability of the Treasury and the Federal Reserve Board in connection with pursuing the method that you advance as a solution, of pumping out sufficient new money and its twin brother, credit, when things slow down, and attempting to control it when things are going out of hand on the up side.

I assume that in your judgment you do not believe that our present mechanism in the field of finance is sufficiently controlled by statute, acts of Congress delegating that power to the Treasury and the Federal Reserve Board, and therefore I must assume, if that is the case, that somebody else must have that final power to make for that shift in the outlook of the banking fraternity of the United States.

Would I be embarrassing you if I were to assume that you may share the opinion that we have that control now, but not exercised by Government? Do you believe there is any institution in the country, any combination of institutions in the banking field, that have sufficient power to bring about the flow of money and credit when, as, and if it suits their desires, and to shut it off likewise when, as, and if it suits their desires?

Mr. Angas. I think that I have your question, sir.

Mr. McKeough. I will confess it was ambiguous.

Mr. Angas. If you will allow me to say so, I think it was a most brilliantly presented case, which I will do my best to answer.

On your first point, I am of the opinion that recutting the cake in favor of the profitor during a slump is a method of ultimately making it grow larger, because it restores profits and confidence, even though it may be at the expense entirely of the wage earner or partly shared with the fixed income classes who own the overhead charge position. So, on the first point, I do agree that recutting the cake can make it larger ultimately, because when you obtain ample profits for most efficient employers, the real national income in terms of goods, sales in terms of money, will then begin to increase again

Competition for men will again take place among employers, money wages will rise, and those wage earners themselves will, with a small time lag, after their wages have been cut, once again get higher money wages and higher real wages on account of the general scale of production being once more increased, and the whole revival can possibly be financed after confidence has been restored by the temporary revival in profits through cutting wages by temporarily hoarded money going back into the situation and things circulating as they did before, despite what might have been a purely psychological check.

The second point was as regards 1929, when profits were high. Was it a healthy situation? Yes, sir; in my view, entirely healthy. Profits were good, therefore production and employment were good. Money went to work. Therefore men went to work and there was no unhealthy price list dislocation element, because the general scale of prices was not rising rapidly. In fact, it was slightly falling. The result was that money was stable in value, which is one of the important ideals. It was stable in value, in general purchasing power, with neither inflation nor deflation, and the mild fall in prices which took place was due largely to technocracy, I think, something which I greatly admire. It is progress in the technique of improvement.

As regards your new era point, I have spent my life since the war in maybe the childish ambition to see in my time new eras, two chickens in every pot. It seems to me entirely possible, now that we have solved the problem of production, that it will occur when we have solved the problem of distribution, and we had a taste of that in America in 1923 and 1929. It can occur again. I believe it will occur again as soon as not necessarily this bill but some bill with similar monetary ideals is adopted and, not only adopted, but practiced.

Your fourth point is what caused the 1929 slump. In my view, that slump in America was caused by the normal cause of business cycles which I discussed at the very outset of my evidence yesterday, namely, the banks only having a certain amount of reserves, prosperity increased until more and more credit was demanded from the banks, despite there not being a rising commodity price level, purely for financing business, but at the same time wages were rising, and so was retail trade, so that much cash was required from the banks for wage payments and pocketbook purposes and for retail trade.

In other words, the banking structure became strained in relation to reserves, and many banks were rediscounting with the Federal Reserve. From a monetary point of view, it had reached a point where very little more credit could be given, and when in any country, as in my country in the last month or two, people in general begin to believe that there cannot be much more expansion, and it does not matter whether their belief is logically sound or unsound, if they believe it the more cautious element in the country says, "We had better get out and take in our horns and maybe get liquid."

Why, America was so prosperous in the 1926–29 period——

Mr. Goldsborough. May I interrupt right there? I live in a rural district largely, and I may say that from the 20th of May, 1920, up until 1936, the rural communities of this country became constantly worse off, and from May 20, 1920, all through 1929, basic commodity prices insofar as agriculture were concerned were constantly falling.

Mr. Angas. Partly technocracy.

Mr. Goldsborough. So that this prosperity which existed in the minds of people whose paper profits were large was apparently a purely imaginary process.

Mr. Angas. I am not sure, sir, that the introduction of manures and tractors on farms, although leading to a fall in farm income——

Mr. Goldsborough. But the prices were actually falling.

Mr. Angas (continuing).—was also accompanied by a fall in farm costs, so that possibly things were not so bad from the point of view of the production of the farmer as may appear from the fall in the price of farm products.

Mr. Goldsborough. I do not know how much practical information you have. I have that practical information, and the farmers have been getting poorer up until 1936 ever since the 20th of May 1920, when the Federal Reserve Board started the process of deflation.

Mr. Angus. I do not say that some industries were not producing too much in relation to effective demand. It may have been true in your area of farming, and in others. That may have been. I am not disputing that. Do not believe that I do dispute that possibility of some industry, even a big industry like farming, over-producing in a new era. They will.

Mr. McKeough. May I bring you back to this control of the money supply, outside of the control of Government?

Mr. Angas. That is the next point, as to whether or not the slump in the fall of 1929 had anything to do with money. That was your sixth point.

Mr. Goldsborough. Wasn't your point whether or not that was deliberately brought about?

Mr. McKeough. I will ask that later.

Mr. Goldsborough. I thought that that was your point.

Mr. Angas. That is the seventh point. The sixth one was, was there a fall in money?

The so-called boom, which was not unhealthy in trade, was financed largely by the influx of gold so that credit could expand with the medium of exchange demand, and the influx of gold enabled the supply of bank credit to be adjusted continuously upward to the growing trade demand. What was unhealthy was that the channel of injection—and this is where we get back to the philosophy of this bill—the channel of injection was wrong—not the volume was wrong;

the volume was right, that bank credit should be expanded to 55 billions, but the channel of injection was the most dangerous possible, namely, 7 billions being lent short through the stock exchange, before it passed on into industry, either on the consumers' or the producers' side.

Let me explain that when a speculator borrows $1,000 to buy some share, like radio at $140, he gets the money from his bank.

Mr. McKEOUGH. That is "prudent" banking.

Mr. ANGAS. On the quality theory it was, according to accepted principles, a sound loan, because the margin was 100 percent extra. From a national point of view, I think at the time it was also desirable to expand bank deposit currency, because trade deserved it. Prices were not rising. When the speculator borrows $1,000 to buy shares, the seller of the shares, unless he buys other shares, which is the same thing—eventually the money comes to somebody who does not buy other shares, and who either hoards it or invests it in a new issue, in which case it goes into industry on the producer's side, and from the company that floats the new issue, it pays wages and buys materials.

Alternatively, it can come into industry on the consumer's side, if the man who sold radio at $240 buys his wife a fur coat, or a new automobile; the money goes into industry.

It is a fallacy to say that loans made to the stock exchange divert money from industry. It appears in the bankers' books, because it is a security loan, and actually it flows into industry, either on the producer's or consumer's side, unless it happens to be hoarded by a nervous man.

What was wrong with the process is not the volume of money. That was good. What was wrong is that it went in through a channel where a mild alteration in price, namely, the price of radio shares, would upset the confidence of the banker and possibly make him call that loan, so that the speculator had to try to get the money from somewhere else to repay the bank, and see what happened. When fear did overcome the market, both the bankers and speculators—the bankers in 1930 called in $4,000,000,000 of short-term stock exchange loans in 4½ months, which could only result, unless there were money measures to increase the supply, in the most disastrous effect on trade, because when the poor speculator had already had his loan called, he had to sell his house or car or mink coat to get money to pay back to the banker, which was canceled, and the bank deposits were canceled. There was a deflation of 27 percent, and the crazy part of it was that the injection was through the speculative channel. It is bad enough today, with the injection through the bond market, but the channel of injection, if subject to nerves, may lead to tremendously rapid contractions of the total supply of money at a moment when theoretically and rationally the supply of money should be increased so as to satisfy the hoarding demand due to fear.

That is what happened in 1929. What should have happened in the slump at the beginning was a positive inflation of money. But inflation has various meanings. As I said yesterday, inflation has 22 meanings to me, but they are wrong to call it the 1929 inflation in terms of inflation of a total supply of money. It was an inflation of stock-exchange loans. If that money had been loaned through a less dangerous channel, you would not have had that huge calling in, or huge deflation.

To be personal, if I had been in charge, I would not have allowed the deflation of the quantity of money to continue. I would have gone in for a gigantic open-market operation, to increase the supply of money greater than the 55,000,000,000 which existed at the peak of the boom. I would have counteracted the fear. There was nothing unhealthy in American industry. It was a healthy new era. Money was not at fault, except the channel of injection. It was nobody's fault. Certain stocks may have been too high, but economically the money was wanted for trade reasons.

Finally, is there a group of men in existence who suddenly decide things are too high, and who call in loans after perhaps having sold their own assets at the top of the market, and thereby create a general slump? In fact, is there an omniscient "they" who go on lending cumulatively to finance a boom, and then at a given moment these 100 men you mentioned, or maybe 60——

Mr. McKeough. I did not mention any number.

Mr. Angas. I beg your pardon. I was wrong. But, referring to this group whose existence you mentioned the possibility of, do they exist? Is there "such an animal"? Do they plan to boost things up, then to bang things down, so as to acquire a greater ownership of the Nation's wealth themselves?

It is entirely possible, in my view, that such a group should exist, but it is customary among many critics of the capitalist system to say, as I said yesterday, that banks on the quality theory of credit and any banker in this room has been trained in it, lend more as prices rise, and as the outlook looks better and that helps to send things up, he lends still further, until the tug comes on reserves. Then the bankers call in, and that sends thing downward, and they call in more, and it looks on paper as though there was a "they," a group of either national bankers or of international bankers who do it deliberately.

I have been—I won't say privileged, but I have enjoyed meeting many of the leading bankers of the world. Most of them are kindly men. Many of them are downright ignorant men on the general problem of the trade cycle, although doubtless good bankers from the point of view of lending, most of their time having been devoted to mathematical calculations as to whether lending 100 units on radio standing at 240 is a safe loan.

I have also met men who I believe to be malicious and unsocial, but my general opinion is that there is not a highly intelligent banking or other group of speculators who deliberately pursue a policy of creating the ups and downs so as to exploit the two movements.

Mr. Goldsborough. I have no doubt you are correct in that statement, but undoubtedly there are groups of men who form pools and who build up the market, and as the market is built up, they gradually unload while they get the public in, and then let the whole business go to smash.

But that is not what you are talking about. You were talking about the general situation.

Mr. McKeough. I was attempting merely to get the benefit of the opinion of the witness by reason of his profound study of the monetary systems of the world, and I would like to go back for a moment——

Mr. Angas. May I finish the answer to your question, which relates also to your statement, Mr. Chairman?

I have seen men at the head of the banking systems grow up—I have grown up with them. I know them intimately, some of them, and many of them are not clever enough to do this on purpose. They do not understand the system. They are busy bankers, lenders, and discounters, and actually they seem as though they were doing it according to plan, but they do it by accident in accordance with the quality theory of credit.

As regards pools, I think that they are immoral. I do not approve of any sort of pool whatever, except the pool created during the early issue of a security in order to look after the price, before there is any market for it on the stock exchange. I think that that is not an immoral pool. All other pools in my view are unsocial, unethical, and shameful.

Mr. **Goldsborough**. And it is a common practice. There is no doubt of that.

Mr. **Angas**. It may be, but I disapprove of it. Speculation, I think, has social values which I need not go into here.

Going back to the question of the groups starting this, it is a fact that they do. When really rich men or important men like bankers, or even investment counsel, who have a following, tell their clients or friends that they are nervous, and explain why they are nervous, maybe because bank reserves are strained, or if you give a dinner party to 100 people at Palm Beach, or to 10 people at Palm Beach, and give your reasons for thinking there is going to be a slump, as indeed happened in numerous cases last winter, 1 man can spread a thought among 10 men, and those 10 men can give dinner parties and spread their thought among 100 men, and the thought, if convincing, can spread like wildfire and create a desire to get liquid, to get out, and the people who do it are often the people closest to the banking-industrial picture.

Mr. **McKeough**. There is room for suspicion.

Mr. **Angas**. There is room for suspicion; there is room for suspecting that which obviously may happen, just like it looked to Galileo that the sun went around the earth.

But knowing the gentlemen who are supposed to be guilty, and having seen their accounts, their deposits, their stock-exchange accounts, they must be given credit for taking an amazing number of losses by accident.

So I do not think that "they" exist to any appreciable degree, sufficient to attract Government attention, although their actions create the slumps which deserve Government or managed-money attention.

Those are, I think, your seven questions, sir.

Mr. **McKeough**. May I ask one or two more?

Do you remember the scarcity-of-money situation that existed in this country in 1907?

Mr. **Angas**. No, sir; I do not. I have studied it a little.

Mr. **McKeough**. You have encountered it in your studies?

Mr. **Angas**. I have studied reports of it, but my age is 45——

Mr. **McKeough**. I hope that you live 45 more years—but that one is at least rumored as having been brought about and having ended by reason of a certain transaction in which a large banking house in this country was interested. I would rather not identify the name. I am sure you are familiar with it, but as a result of that, a certain institution whose name I have referred to, Big Steel, took over Tennessee Coal, Iron & Railroad Co.—do you remember that?

Mr. **Angas**. No, sir. I should, but I do not.

Mr. McKeough. Then the panic ended, and the scarcity of money was finished. It was that situation I think in the main that brought about the enactment of the present Federal Reserve System in 1913.

Now, the head of that banking institution has since died, and his son, who now conducts the business under the same name——

Mr. Goldsborough. Nobody has the slightest idea whom you mean. [Laughter.]

Mr. McKeough (continuing). Strangely happened to land in London the day England abandoned the gold standard, and I think that you were at least interested in the stock market at that time. The announcement came in the early morning, on Monday, and there was great fear that the New York Stock Market would not open, but it did open. That market went off very heavily for the first few hours of that market day, but it finished and sold higher at the close than it had at the close of the preceding Saturday; and maybe I pay these gentlemen too high a compliment, but my contention is, Major, that there is a certain "they," and I do not know who they are, but I have a suspicion of at least the identity of maybe one or two of them by name, for things do not happen, even in money affairs, in my humble judgment, but they are brought about, and if they are brought about, somebody initiates the move, and I even go so far as to say that I believe these unknown "they" even make and unmake governments.

I recall one incident that related to the rather hectic activities of a gentleman that came originally from Sweden. Kreuger was the name. He died—at least, his death was reported. He did a lot of business for the Swedish-American Match Co., and he told us at a meeting at which I happened to be present, in answer to a question as to whether or not the Swedish-American Match Co. was doing well—he said, "We are doing very well. We just finished a contract with the Government of Peru." He said: "We had some difficulty in making the contract; in fact, the President of Peru had to discharge the secretary of state, who refused to sign it. We were very much annoyed by reason of that unhappy situation, so that when we made the contract ultimately with the country known as Peru, the result was that they now pay more for their matches and have fewer matches in a box than any other country that we do business with."

He said: "We just finished a contract with Poland, under the terms of which we get all of the standing timber suitable for the match industry in Poland, and all of the sulphur deposits. We had some difficulty in getting that contract through the Polish Parliament; in fact, we only finally succeeded in passing it with a margin of one vote."

You are familiar, I am sure, with the fact that he arranged with the Government of France to make a loan to France for the outstanding 7's and 8's floated here in this country by the French Government after the war, whereby he made an agreement with the Government of France to take over a 50-percent monopoly in the 100-percent French monopoly held by the Government of France in the match industry. He loaned France $50,000,000, with which they called the 7's and 8's that were here in the United States, and then he borrowed $50,000,000 from the rather widely known house of Lee Higginson & Co., and he gave Lee Higginson & Co. some promissory notes known as the Swedish-American match debenture 5's.

Now, if Mr. Kreuger were able to finance activities of that nature in Poland, Peru, and France, my suspicion is that older banking houses and operators certainly must have enjoyed similar power. In my own country, the Tennessee Coal, Iron & Railroad Co. was taken over by United States Steel, and the money scarcity of 1907 was ended. Morgan landed in England on the day England abandoned the gold standard.

So I am a little bit suspicious, and I am also suspicious because, somewhere in the United States, strangely, there was a slowing down of industrial development in the year 1937 in spite of the growing profits of industry, which resulted in a marked slackening of industrial activity, and, as you may recall, action was taken by the administration in charge of this National Government at the present time in connection with an unemployment census, to get some definite idea of the actual number of people who sought employment and were able to be employed if given the opportunity, so that in the deliberations of the administration and its effort to meet the growing problems inherent in our depression, it wanted definitely to know how many people were out of work.

As you know, they got that machinery under way, and it took about 90 days, so that the date was set for about the middle of November past. But my suspicion now comes to the front, and indeed I am a little bit inclined to think that that was about the high point reached in unemployment up to that particular period of the 12 calendar months that make up the year 1937. The steel industry was moving along at a pretty rapid clip——

Mr. Angas. Did you say in unemployment?

Mr. McKeough. In unemployment up to November. It has since enlarged, but it grew with a rapid development between September and the middle of November, when everybody knew by reason of the fact that the press carried the announcement that as of that date cards were to be passed through the Post Office Department and everybody out of work was to fill in a card, with the result that if I were a part of that movement, I think I would probably have been better prepared in the middle of the month of November to make sure that my plant looked like it had no further use than I would have been if I had not been advised prior to that, and it may have been political; I do not know, but if your philosophy is sound, and I have no quarrel in many respects with it, I must begin to differ with you that the profit enlargement is the answer, unless some new mechanism may be introduced by governmental action to control by Government the outflow and intake of the money issue that will make more difficult at least the ability of those that now are able through bank collections to call loans, tightening the credit and retrenching the activity of money, and if you agree that the Government should take that responsibility, I would have less quarrel with your philosophy than I would if you desired that the present rugged individualistic philosophy were permitted to take that responsibility and not answer to the Congress as to whether it performed it well.

Getting to Mr. Goldsborough's principle, I think as you do—I think you referred to it rather as a branch in the approach to this condition, instead of the trunk or the roots of a tree—you used the word "branch"?

Mr. Angas. Yes.

Mr. McKeough. I am making it apply to the tree. If we had the control in the roots of the tree, this governmental agency would attack slumps by the issuance of additional money, and I think that we would then make a constructive approach in our attack on the economic distress and the economic booms, but it must be a governmental agency, in my judgment, answering to the people, definitely and conclusively, taking the full responsibility for their activities in the reports that they render to the agency called government, the representatives selected by the people of the country to go and represent them and their interests at the National Government's headquarters, and I would like the record to definitely show that I am convinced in my own mind that these hectic booms and terrifying depressions are more or less artificially manufactured by that unholy controlled still invisible "they."

The one hopeful sign that I see is that recently I have read in the press where the United States Steel Corporation has again entered into a contract with a labor organization to maintain the wage structure in its plants throughout the country, and I know of no more hopeful sign as to the immediate future in the way of industrial pick-up than to have read that, followed immediately in 48 hours with an announcement that General Electric likewise has made a similar contract.

Now, I subscribe to the philosophy that we had better give it to the fellow down below first, and if it is necessary for that phrase that you used, the "time lag," in order to get the industrial activity going again, let him who has the most hold the responsibility of the "time lag," rather than the fellow who has less, because the fellow who has most obviously can better afford the "time lag" liability before his return develops to him, and if you can get the answer to that, coupled with Mr. Goldsborough's philosophy of giving that purchasing power to the millions who are dependent on the whims of the invisible "they" as to whether or not they can work, then I join with you most wholeheartedly, and I think that that is the answer, in the main, to the effects of the depression, that the situation can best be handled by an attack on the root of the tree, which is the monetary system in full control of the Government, responsible to the people in a democracy such as we have.

Mr. LUCE. May I ask my colleague one question?

Mr. McKEOUGH. Surely.

Mr. LUCE. Just 100 years ago the country was in the throes of a depression that probably was more serious in proportion to population and invested capital than that which is now going on, and as far as United States history goes, there have been such periods for a century or more; they have averaged about every 20 years. Does the gentleman think that those were artificial in their causes?

Mr. McKEOUGH. I will say, Mr. Luce, that if there is anything in my suspicion, that relatively I must be suspicious of those. One hundred years ago we were a nation of agriculture. We were a borrowing nation, a debtor nation. The industrial development of this great country of ours was on borrowed money, in the main, from Europe, and we were more subject, in the event that this ability rests with those that have control of capital and money, by reason of our being a debtor nation, than when we became a creditor nation, but the control still rested in the same group, so that, if I am justified at all in being suspicious, I must of course continue to be relatively so for any period in the history of the Nation.

Mr. LUCE. Then do I conclude that you think it is about every 20 years that a group of scalawags gets formed?

Mr. MCKEOUGH. No; I think that it is not just metered out in equal measures of time. We had such a situation in 1929 and 1933.

Mr. LUCE. I am talking about the big depressions.

Mr. MCKEOUGH. It is thought by some the one we are in now may develop into one.

Mr. LUCE. It is a new theory on the cause of depressions.

Mr. MCKEOUGH. May I interrupt just a moment, Mr. Luce, and offer this thought, that our witness has indicated repeatedly the mechanism which prudent bankers should follow. I am not mad at the banker. I trust that whatever remarks I have offered will not indicate that I am hopelessly a "parlor pink," or a Socialist, or one who agrees with their philosophy of complete state control over its people. That is all anathema to me. I do subscribe, however, to this philosophy, that a nation as great as ours, providentially endowed with the richest natural resources that any country, with the rare exception, possibly, of Russia, possesses, and we differ from Russia in that we have developed ours, we are certainly an impotent institution if we must just accept the determined idea, predetermined, that we cannot do anything about this, that we must suffer these periodical depressions without in any way creating a cure, and I go so far as to be willing to be looked upon as unorthodox, as the witness has referred to it, by saying, "Let us change the capitalist system for something that might be better, if we otherwise must have these periodical depressions." I think that there is no justification for 130 million American citizens being subject to these conditions being visited upon them, through no fault of their own, every 20 years.

Mr. GOLDSBOROUGH. Or any other time.

Mr. MCKEOUGH. Or any other time, and I say that if we are worthy of the rich traditions that are ours as a nation, we in the Congress ought to have the answer, somebody ought to have it, and I am hoping we will get it, and I am willing to stay up 24 hours a day from now until the end of the year, if I could stand that physically, in my humble contribution to making it so.

Mr. LUCE. I share that hope, and I am not at all at odds with the gentleman on that, but it is simply a question of whether it is true that depressions are due to the machinations of a few men.

Mr. TRANSUE. I would like to ask the witness if he is familiar with the facts set forth by Charles Morgan Webb in his book in regard to what happened in 1929?

Mr. ANGAS. I get rather muddled over his silver policy. I cannot understand it.

I read his paper. He sends it to me.

Mr. TRANSUE. My question is whether or not there had been a management of our currency by the Chairman of the Board of Governors, by Chairman Strong, from 1922 until about 1927.

Mr. ANGAS. I think he did very good work.

Mr. TRANSUE. And that about at that time the policy of management of the currency did change, but there was an inflation brought about by speculation, and that culminated in the one day in October when the collapse came? I want to know whether or not you agree with his analysis of the situation.

Mr. Angas. I never knew Benjamin Strong, but he seemed to me to be attempting to carry out with the few powers at his disposal whatever good he could.

Mr. Goldsborough. Mr. Luce and I remember distinctly a number of times when he was here before our committee. He believed that stabilization of the price level was nearly a cure for our monetary difficulties. Where Mr. Strong differed with certain members of this committee was that he thought it ought to be left to human ingenuity to decide what to do. Some of the members of this committee felt that it ought to be written into the law that the Federal Reserve System should use its power for the purpose of maintaining a price stabilization, and he objected to legislation, but as he was not immortal, and as the legislation was not passed, when he died the whole policy went to pieces.

Mr. Angas. That is what appeared to me, but he was not given to many statements, if I recollect rightly.

Mr. Goldsborough. He testified very freely before the committee.

Mr. Angas. The honorable member of the committee asked me a question which I should like briefly to answer, concerning the possibility of hidden hands creating booms and slumps to their own advantage.

That possibility undoubtedly exists, and I agree with him that if such unsocial behavior occurs, it is desirable to prevent it, maybe by the Government, maybe by the Securities and Exchange Commission; I do not know what technique should apply; but even if that exists, there still remains the other problem of the trade cycle which I have discussed, which itself gives scope for men of that mental temperment to practice these forms of financial behavior.

I hope, and I do not know your name, sir——

Mr. McKeough. McKeough.

Mr. Angas. That the gentleman will go with me so far that even in a country where there was no such group, that the problem of the trade cycle still remains or may remain. Whether such a group exists in this country, I do not know; I have often wondered. In my country I do not think there is such a group. The 1929 depression in England was attributed to the Hatry collapse, and by other people attributable to the collapse of the Austrian bank called the Credit Anstadt.

My problem of the trade cycle still remains, even if there is the additional problem of social morality among certain groups, so I hope the honorable member will not condemn the case I have been trying to make just because I have not emphasized the possibility of some slumps being caused by manipulation of men of great power and influence.

I say that because the honorable Member said that he would go with me further in my views if I held his views, or words to that effect, but I hope he will separate in his mind the two problems, the one having to do with the trade cycle in a country where there is no bad morality, and the additional problem of a group with bad morality, so as to keep either from supplementing the trade cycle disease or maybe even creating it.

Mr. Goldsborough. Major Angas, I do not think that the thing you speak of is at all uncommon. I doubt very much whether a wholesome condition can be created by any group of men.

Mr. **Angas**. It cannot right any values, in my view, but it can be done by bankers, and I mean by speculators who have not got control of the banks. I do not think that the general trade cycle can be appreciatively effected by them unless they have the money power, either directly as bankers or through having control over a large number of banks. In my country there are only five, and taking one big bank, the bank which my own family founded, if the directors of that bank decided to sell all of their investments, all of the bank's investments, and to call in a large part of the loans, they could lower the price level in England by 20 percent and create a stock-exchange run.

I do not think one banker under the cash-reserve system can cause inflation, but since bankers in my country are few in number, a single one of the big five can undoubtedly cause a panic. The power is there.

Mr. **Goldsborough**. Gentlemen, it is now 25 minutes of 2, and, without objection, the committee will adjourn until half past 10 tomorrow morning.

(Thereupon, at 1:35 p. m., an adjournment was taken until Wednesday morning, February 23, 1938, at 10:30.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

WEDNESDAY, FEBRUARY 23, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:40 a. m., Hon. T. Alan Goldsborough presiding.

Other members of the committee present:

Mr. Reilly; Mr. Williams, Mr. Spence, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Transue, Mr. Barry, Mr. Gifford, and Mr. Luce.

Mr. Goldsborough. The committee will be in order, please.

We will be very happy if you will resume, sir.

STATEMENT OF MAJ. L. L. B. ANGAS—Resumed

Mr. Angas. Well, sir, I have said about all I have to say on the principle of the cycle and the preliminary argument which I personally think is necessary for such a bill as this, and I presume today I shall be asked a few questions. I admit there are many points on this problem on which I have not touched. In being asked questions, because of the fact that I am a foreigner in a country which I very much love, I am in a somewhat difficult position, because if I say anything against the bill, I will be accused of trying to destroy something to help the American welfare, whereas if I say anything in favor of the bill, I will be accused of being an impertinent Englishman who comes over and tells you what you ought to do; so I am very nervous, and, Mr. Chairman, I hope that you will not press me to say anything which will be reported that can put me in this rather dangerous international position, because I am very anxious to improve rather than aggravate international relations. Indeed, I do not want myself either to defend the bill or attack the bill, and I do not particularly want to be forced into trying to explain the bill. I am not its father, although some points on it I might possibly be able to throw just a little light on.

As regards the administrative details of the bill, here again I am a foreigner, and if any of you gentlemen went down, shall we say, to Peru to give an opinion on what would work on the administrative side in Peru, I think that you would be rather reluctant to say what could be done and what could not. I feel the same as a very fortunate visitor to America. I may have my ideas and make guesses as to whether there would be difficulties, but I am reluctant to be at all dogmatic on the administrative question, particularly out in the country, on the circumference of the administration, although I am perhaps very dogmatic about the problem of the trade cycle and its potential cures, which is a thing that I have studied.

So I would ask you not to demand from me an explanation of the ultimate details of the administration in each congressional district in the United States.

Yesterday I was asked a question but was unable to complete my answer to it, because another question was immediately put to me, the second question being a long one, so that I did not complete my answer to the first. I was asked, is the bill inflationary? I said yes, it is inflationary, and then I paused. It was a full stop or period in the sentence, and I was going on to say that it was also deflationary, and that indeed any bill which is going to manage money effectively must have teeth in it to prevent price inflation as well as force behind it to create price inflation, a quantity of money inflation. I was unable to finish that statement, and I find my name in the press as being an inflationist, as usual—I, who have written two books on the general question of what is going on, which are perhaps more anti-inflationary in tenor than any book I have ever read by anybody else. Such is the unfairness of the world, when one tries to preserve the balanced view, realizing that the driver of a car must be able to turn that car to the left and the right instead of in one direction only.

I have also read, besides the bill, I believe the whole of the evidence on the bill, and in running through it, there seems to me to be a lack of distinction between a slump due to inadequate purchasing power, in the form of money, and a slump due to inadequate purchasing, and they are as different as night and day. The present slump is not due to inadequate purchasing power or quantity of bank credit money or any other money. Just the reverse. There is plenty. It is due to inadequate purchasing, and yet running through page after page of typewritten matter I have read on this, there seems to be confusion, so please allow me to draw that not very subtle distinction, as I see it.

Mr. TRANSUE. Would you care to amplify these things as you go along? What I am getting at is your statement that there is ample purchasing power. I would like to have you explain that a little further, in view of the fact that we have, as the unemployment figures show, may be 10,000,000 people who are unemployed, and to ask you where their purchasing power is.

Mr. ANGAS. All right, sir. I will attempt to amplify it.

The volume of bank credit money in this country today is just about the same as in 1929 and also in 1936. It may be 10 percent different, but it is about the same, and, looking at the total quantity now as regards its distribution, if trade could be very brisk in 1929 with this amount of money, and in 1936, there is probably enough money today to have trade as good as in 1936 or as good as in 1929, given certain conditions which apparently since last August are now missing.

There is a little money missing, a deflation of 6 percent, but the deflation of trade is nearer 30 percent. I think that there is enough money in existence today, bank money and other sorts, to have very good trade; in fact, rather even a wild inflation given certain conditions of confidence, but the confidence is lacking, and the velocity is lacking, because of fear. In other words, the store-of-value demand or liquidity demand has grown very rapidly in the last 6 or 8 months, whereas the supply has not grown very rapidly and the hoarding or velocity factor has caused the slump.

I say that there is enough money to haver certain conditions today, and I ought to have added that qualification more clearly earlier.

Mr. Transue. Have you completed your statement?

Mr. Angas. I want to add an important remark if I may, please, sir.

My solution to a condition where an increased store-of-value or liquidity demand for money matures, no matter for what reason—one of my solutions is to increase the supply of money parallel with this increasing store-of-value demand or with the decline in velocity, whichever term you care to use. In other words, I want to inflate the quantity of money or the supply of money parallel with the psychological increase in liquidity demand, and that incidentally when done or even the threat of it tends to stop the hoarding and to make money flow with its normal speed again. Quite simple.

Mr. Transue. Speaking ——

Mr. Angas. People say to me then, "Oh, but there is plenty of money about, and banks are simply bulging with it. There is no demand for it. Your solution, therefore, must be crazy."

But such gentlemen confuse the loan money market and the demand for loan money, new loan money, from the banks, as I emphasized yesterday—they confuse that demand for loan money with the demand for deposit currency. It is a subtle distinction, but something entirely different. There is the loan market, which is absolutely glutted with loan capacity, and the demand for new loans in relation to the supply possibility of new loans—that demand is very low, but the demand for money as a whole in circulation, already in people's pocketbooks, and passing through trade, is very slight, because of fear. Everybody is investing in it. I have been until recently advising people to invest in it myself, to get liquidity, and when people say, "Oh, but the banks are glutted with money," they are missing the whole point. They hoard it, and do not pass it on.

Mr. Transue. You spoke of the fear element and the lack of confidence, which is another way of saying the same thing. In connection with the change in 1936 or 1935, when did that fear or lack of confidence start, and what is its cause?

Mr. Angas. I will try to word my answer without treading on any august toes.

You had a very interesting condition in this county, to me. You had a huge 30-percent inflation beginning in 1934, with Government expenditures financed by borrowing from the banks. You had in fact a vast increase in the supply of loaned money. Net demand deposits unadjusted of the reporting member banks rose from 8 billion at the bottom of the depression to an equivalent now of 17 billion unadjusted, double for the reporting member banks. If the other banks moved parallel, it was virtually 100-percent inflation of net demand deposits, and yet you never got your 100-percent inflation and you never got trade as high as 1929. Why? Because fear was created among a great many people that what was happening in America was unsound, and they tried to keep liquid all the time. A great many men were afraid, if you like, of the governmental policies, and certain Washington speeches added to that fear, particularly when it came to social reforms.

There were other factors than Washington speeches, like strikes in Detroit in 1937 which, from a monetary point of view, brought about the result that you had an increasing hoarding demand for money, due to nervousness, to social reform, and other things occurring at the same time as the bank credit inflation was occurring, so that prices did not rise very much, although they might have if confidence had been like it was, say, in England, where the relatively rich and the relatively powerful were not frightened of governmental policies.

Looking at it as an Englishman, I have put this in words, so that it does not much matter my repeating it; I have written this in pamphlets. The curious monetary feature of the Roosevelt administration has been that, although he has done a vast amount to increase the supply of money, which action has a tendency to create a trade revival and a boom, he has simultaneously seen growing in his country a state of mind among businessmen which has stimulated the public demand for money, not loan money, as fast as the supply has been increased, so that that is why the inflation has not caught. If you like, the quantity of money was turned on by the administration to make trade better, but the words of the administration slowed down confidence and checked the improvement and inflation of prices that would otherwise have occurred.

That is what happened.

Mr. Transue. I want to follow that just a little further by asking you this, to explain to me why, if this fear or lack of confidence results in our present condition, the automobile industry went through one of the best years they ever had after the labor trouble had occurred. Does it take 8 or 9 months for that fear to catch up with them?

Mr. Angas. Your trade did not stop falling much statistically until about September. The stock exchange slump began on August the 18th, to be precise, and trade began about 3 months later, going down fairly fast, but after a pretty good year, in the first two quarters, and a very bad third quarter.

I am not quite sure of the purport of your question, sir.

Mr. Transue. What I am trying to ask you is this, That if the fear or lack of confidence is what is holding up business, why was not that element present in 1936 and 1935, when it seemed to me that we were getting a better condition all the time, and why, if the labor difficulties caused that fear, it did not take hold until 8 or 9 months after it happened.

Mr. Angas. That is a very reasonable question.

The answer is that the fear was present the whole time, as you say. I agree, and, as I say, not because I am putting words in your mouth——

Mr. Transue. I did not say it.

Mr. Ford. Do you think it was an intelligent fear?

Mr. Transue. Just a minute. I did not say that I believed that the fear stopped the business.

Mr. Angas. No; you were quoting me, and I was requoting you. I undo all that backward.

As I said, the fear was there all through the social reform period of 1935 and 1936, but trade kept on advancing, largely because money was being dumped into circulation in an inflationary manner all the while, thus conteracting the positive effect of the fear. When they stopped pumping in the moneys quite so fast—it may have been chance, but the fear got the upper hand over the quantity of money. In fact, statistics support that view that when bank money stopped expanding itself, when the banks began selling their investments and the inflation stopped or slowed down, then the fear began to get the upper hand, first over the stock market and eventually over trade.

Mr. Transue. I just want to ask you one thing further, and that is this, that it seems to me that factories run when they have orders for their products, and when they no longer have orders they shut down and lay off men. It seems to me further that if these factories had orders today they would make their product and sell it, but that some place in there they quit where the orders stopped. Was that due to fear on the part of the potential consumers, or was it due to the fact that they did not have any money with which to buy?

Mr. ANGAS. Is that the end of the question?

Mr. TRANSUE. That is the end of the question.

Mr. ANGAS. Both.

Mr. TRANSUE. Now——

Mr. ANGAS. I will continue, but I want to give a fairly carefully worded answer. The initial cause of the cessation of consumption was very largely due to fear among a relatively small group, and their actions, their fears led to actions of a cautious nature from a business and investing point of view, and that cautious action prevented them from spending money which they controlled, and they kept it idle.

The secondary reactions from their primary action were that some of the public who were consumers, to use your word, went without incomes, and therefore, they as individuals, from a point of view of distribution, lacked purchasing power because their incomes had stopped. Other people had the monetary purchasing power, but their lack of confidence prevented them from passing it on, thus checking monetary velocity, and that is how it happened, in my view.

Mr. TRANSUE. These few that you speak of, that you say originally had fear, are those the few that have the control over the larger amount of savings deposits, as compared with about 98 percent of the people having about one-third of the money in savings deposits now?

Mr. ANGAS. What do you mean by savings deposits?

Mr. TRANSUE. Savings or commercial deposits—money in banks, I should say.

Mr. ANGAS. Do you mean current net demand deposits?

Mr. TRANSUE. Yes.

Mr. ANGAS. On the whole, in my view, it began with a minority, perhaps with the minority who were most frightened of the policies of the present administration, who are composed for the most part of men of wealth, both in Europe and in America. They were also frightened, many of them, of something else, namely inflation itself, but if you are frightened of inflation, you spend all the money you have got, and try to get rid of it and invest it in something else, but when a deflation starts, you stop that sort of behavior and hoard the money itself.

There were the two sorts of fears, fear of inflation and fear of the administration, and first one had the upper hand and then the other.

That is the psychology, as I observe it, one leading to high velocity of spending, and the other to low velocity of spending.

Mr. TRANSUE. Then, to get to the next question, if the people that you speak of had as much confidence as the large bulk of the American people, we would probably be all right today?

Mr. ANGAS. I cannot measure the confidence of the large bulk of the American people. I am not, I hope, trying to score off you by that remark, but you can measure the confidence of those who can control large idle balances by watching the way they behave. It is much more difficult to get statistical evidence of the behavior of those with small idle balances, which are the masses of the people.

Mr. **Transue**. But the confidence of the masses of the people was measured by the fact that they did go out and buy when they had the money.

Mr. **Angas**. Yes, sir; and the retail trade stayed pretty high, which rather supports the view that the confidence of the ultimate consumer, or the lack of fear of the ultimate consumer, whichever you like, was less great than among the controllers of the big investment funds of the country.

Mr. **Transue**. Then I get to one further question. If that ultimate consumer either had the money in his pocket, or an opportunity to get it, trade would be good?

Mr. **Angas**. I agree with the first.

Mr. **Transue**. If he had the opportunity to spend, or the opportunity to get it?

Mr. **Angas**. I agree with the first part of the question, but I do not think the second part follows.

Mr. **Transue**. Well, I take it that it goes without saying that the majority of the people of this country, the same as all over the world, if they have the opportunity to get money, to earn money, will soon be in the class where they will be potential consumers.

Mr. **Angas**. Under that definition, the first and second half of the questions are identical. They have that money.

Mr. **Transue**. I see that distinction, that there are at least 10,000,000 people unemployed, without the opportunity to get that purchasing power which is necessary to make trade and to purchase the things that they need.

Mr. **Angas**. You see the difference in the way you asked the question? You said would the people who had money spend it. That is the first half of the question, with the verb put at the end. The second half of the question was, if they had an opportunity to get it, would they spend it, and the answer is they cannot spend it unless they can borrow somehow, and until they get it——

Mr. **Transue**. You will excuse me——

Mr. **Angas**. I do not want to be at all meticulous——

Mr. **Transue**. I want to try to make my question clearer. If the masses of the people of the United States had purchasing power, or if the masses of the people of the United States had an opportunity to acquire purchasing power through employment, would trade be good?

Mr. **Angas**. If you cut out the word "opportunity," if they acquired money through employment—that word "opportunity," I do not know whether there is a catch in it for me or not.

Mr. **Transue**. All I mean by it——

Mr. **Angas**. Leave out the word "opportunity" and the answer is definitely "yes."

Mr. **Transue**. What I mean by it is a man that wants to work and is able to do it if he gets the opportunity to find work.

Mr. **Angas**. That is another question If you want me to say that if men had jobs, would trade be good, I will say "yes." My only difficulty was with the way you worded your question. I am taking it literally. I think that I agree with you entirely on the aspect of the problem you are looking at. The great thing is to get money into the hands of the worker, or the consumer.

Mr. **Transue**. The ultimate consumer?

Mr. **Angas**. Yes. I am being very cautious, perhaps. I am accustomed to economic arguments. Yes, the ultimate consumer is a very important fellow.

Mr. **Transue**. And if he had that money and spent it, would this confidence return to the upper people, who, through fear, as you say, have been too cautious?

Mr. **Angas**. I am not certain. It might be a funny sort of confidence. It might be a confidence in larger trade. In fact, it might be a lack of confidence in money, but they would go to work and produce goods, I think, if there was a monetary market for them. Yes; definitely.

Mr. **Transue**. I think that is all.

Mr. **Angas**. Definitely, in my view.

Mr. **Luce**. Major, I have listened to your testimony with interest and profit, and with nearly all of your arguments I am in complete accord. My questions, however, will be largely addressed to your bulletin, Digest No. 14, part of which you quoted from, and all of which is in line with what you have testifid.

Mr. **Angas**. I will answer that I may have to reserve on anything to do with the stock market.

Mr. **Luce**. I shall ask you nothing about that.

Following along the questions that have just been asked in the matter of the money supply for the masses of the buyers, I take it that the masses of the buyers in this country do not have checking accounts. Do you agree with that?

Mr. **Angas**. I would.

Mr. **Luce**. That being so, do not the figures as to the money in circulation shed some light on the capacity of the masses to buy?

Mr. **Angas**. Do you mean in terms of notes?

Mr. **Luce**. I mean——

Mr. **Angas**. Do you mean money? I use that word in five different ways.

Mr. **Luce**. I appreciate that, and I will save you the necessity of going into that by saying that I am talking about cash currency.

Mr. **Angas**. That is, notes like the ones I have in my pocket?

Mr. **Luce**. Yes. I assume that the figures on the cash currency in circulation would be an indication of the volume of the purchasing power on the part of the masses of the people?

Mr. **Angas**. Probably; yes; but one cannot quite prove it. It is probable. That is my answer, that it is probable, yes, but not indisputable.

Mr. **Luce**. I will point out to you that in 1930 the money in circulation was given to us as $36.74 per capita.

Mr. **Goldsborough**. What was it in 1929, Mr. Luce, if you have it?

Mr. **Luce**. $51.38—no; that was in 1920. The 1929 figure I cannot lay my hands on, but the cash circulation in 1930, as I have said, was $36.74 per capita. It rose in 1931 to $31.86, in 1932 to $45.61, and in 1933, when the depression was at its lowest, the volume was $45.49, and on the 31st of last December, 2 months ago, the circulation was $50.51 per capita.

In short, there has been all through the depression a steady rise in the cash currency of the country. How do you reconcile that with the allegation that the masses lack purchasing power, if you accept the doctrine that the masses are not often depositors in banks?

Mr. Angas. That is the end of the question?

Mr. Luce. That is the end of the question.

Mr. Angas. The public demand for legal-tender money consists of three parts, of a wage-paying demand, which goes around the corner on Saturdays through the shops and back, and probably the following Thursday, or even earlier, into the banks. That is the normal circuit, or weekly flow. Then the pocketbook demand, the stuff that one carries on one's self for tram fare, trolley-car fares, cab fares, lunches, and so on; and, thirdly, the till-money demand. Those, broadly speaking, are the three chief uses of legal tender, and obviously the more a nation uses cash, as it is loosely called, to pay wages, the greater will be the mathematical quantitative demand for cash notes; whereas if all of the wage earners all used checks, probably there would not be such a big wage-paying demand on money held outside the banks. I do not think that I need enlarge those three demands, except to say that the higher the wages, the greater the demand.

Then, secondarily, as regards retail trade, the more of it being done the greater the amount that your little shop will hold idle in its till as till money, while certainly the price level is important, because the higher the price of cabs or lunches the more one carries in one's own pocket, assuming that one has this kind of money in the bank or money in one's pocket.

Those are the three normal economic demands for notes or cash, or legal tender, as we call it in England, but there is another cunning sort of demand which may creep up, due to lack of confidence in the banks, and whenever a lack of confidence in the banks grows, the people who are frightened of the banks say, "I had better get my money out," and so the statistics of the money in circulation outside the banks rises very rapidly.

Incidentally, there are seasonal changes, as you, sir, know better than I do, but just to round out the statement, there are seasonal changes, like one carries more money when one goes on a holiday, or Christmas, or in the summer, or even when one comes to Washington to give evidence and one does not know how soon he will get away. [Laughter.] That is why I say that the statistics of currency outside of banks prove nothing, although there is a tendency for a higher wage level. I do not mean so much the prices paid per hour on work on the product produced, but the number of men in employment and the money wages that they receive. The greater they are, the greater mathematically will be the quality of money used for wage-paying purposes, and I have been unable in my studies to prove anything by the amount of money, of legal tender, in circulation, becasue of these varying factors.

The motor car has led to a very great increased demand for cash in one's pocket. In the old days, when one never went outside of one's local farm, one did not need very much cash in one's pocket, even if one was a millionaire, but when one goes running about the different places, like Atlantic City, Coney Island, Palm Beach, according to your choice——

Mr. Ford. And Los Angeles.

Mr. Angas (continuing). Because of the motor car and the improvement in transportation methods, that goes on.

To answer your question, therefore, now as I did to start with, I do not think that anything can be proved from the gross quantity figures.

Mr. PATMAN. Will the gentleman yield for a brief observation, not a question?

Mr. LUCE. Yes.

Mr. PATMAN. May I express the hope that the questions will be directed to the bill as much as possible? These are very interesting, and I appreciate them very much. I doubt, however, that the major will be with us very long, and since he is here in connection with a bill that is pending before the committee, of which he made a study last night, I suppose it is important that the questions be directed to the bill, and after the gentleman concludes, I would like to ask some questions myself on the bill.

Mr. LUCE. I am addressing my questions wholly to the principles underlying the bill, and the purposes of the bill.

Mr. GOLDSBOROUGH. Proceed, sir.

Mr. LUCE. One of the main purposes is alleged to be the desirability of increasing the circulation of money. I wish to find out whether that is necessary or not, and, furthermore, I have not had an opportunity for some days to ask questions, and this is the first time that the minority side has had that opportunity.

Mr. PATMAN. I always enjoy the gentleman's questions. He always asks good questions, and constructive ones.

Mr. LUCE. I want to observe that the questions that I have asked are of very grave importance.

Mr. ANGAS. I agree, sir.

Mr. LUCE. Because a presidential campaign was fought on that issue 32 years ago, and there are pending in the Congress various proposals intended to meet the purpose of this bill by printing more money, and so I wish to find out your views in the matter.

Now, then, if we are to assume that Mr. Bryan was all wrong in attaching any consequence to the volume of outstanding cash currency, and that the gentlemen who are now urging Congress, and are putting down their names to the extent of some 160, I think, are in favor of the same thing, it seems to me pertinent to inquire from such an authority as yourself what your views are on some of these matters, and you have just stated, and I am glad that you have said it, because I largely agree with you, that the volume of cash currency in circulation in the United States is not an ascertainable factor.

Now, then, to get on to the next point——

Mr. ANGAS. For the sake of the record, may I add this—in this country. In Germany, or the note-using countries as distinct from the bank-depositing countries, you can have dogmatic views, much more than in a cash reserve ratio country, or fractional reserve country.

Mr. LUCE. Now, the next step in the inquiry is to get a clearer understanding of your use of the word "hoarding," which in your digest and in your remarks you have frequently used. "Hoarding" ordinarily has been meant to imply the secreting of cash currency. Its extension to deposits is new to me, at least—bank currency—and I would like to have you make it clear, and let me give you a tangible illustration of what I mean——

Mr. ANGAS. I am very glad you asked that question.

Mr. LUCE. When things were bad in 1933, I directed the manager of the little business in which I am concerned to keep a larger balance in the bank, and I kept a larger personal balance in the bank through fear, not knowing what might come any moment. Now, let us assume that as a result of those two things, the banks held $10,000 of money that I otherwise would have put into productive use——

Mr. ANGAS. Or consumptive use.

Mr. LUCE. Where I find it difficult to follow you, sir, is in the variance from my own logic, when I assume that the bank took that $10,000 and turned it over, if it could, to somebody else who was willing to produce. Now, will you explain to me where I am wrong in that theory?

Mr. ANGAS. I am very glad that you asked that question, sir, because in my evidence I have been using the word "hoarding" without having defined it, and the word is a vague word, and, like almost every word in economics, it has many meanings.

Since there are two sorts of money in the country—namely, notes and bank deposits—there can quite well be, indeed are, two sorts of hoarding. We are all aware of hoarding notes, legal tender. I use the term, as you appreciate, sir, in relation to hoarding bank deposits, like the action to which you referred, when fear induced you not to spend with normal speed. It is usually believed that hoarding in the economic sense involves taking money out of the bank. It is not so in the bank-deposit currency-using country. That is hoarding cash. I have been mainly talking about hoarding bank deposits, which merely means that you do not write checks against them. The banker, if you do not write checks against them, has neither more nor less on the asset or liability side of his account. His loan facilities are not increased, nor are there figures on his books changed one iota except his clearing figures, check clearing figure. He is in exactly the same position.

There is this subtlety, that if you put your money off current account or demand deposit, onto what is called time deposit in this country, and then begin to receive interest, the banker feels a little bit safer in making further loans, becauase he is only required today to keep 6 percent of the reserve cover against time deposits, whereas he is, if he is an outside bank, required to keep 26 percent today. He therefore may be stimulated to lend more or invest more if you transfer your idle balance from demand deposit to time deposit.

But the idea that a bank always lends or invests money that you are not spending for the moment is not true, because if he did he would be increasing his loans at an enormous rate, because money for the most part is, as it were, idle all the time and not changing hands. Strictly speaking, if you are a banker, when money changes hands in your bank, it is when you happen to write on your books a figure, and you debit one account and credit another. It is an idle balance in there all the time.

So your action is a hoarding of bank-deposit money, which will probably not be lent by the bank. It might be if you put it on time deposit. If might be. It might be invested by the bank, but the bank does not know, if you permanently keep it on demand deposit, when you are going to draw a check against it, and therefore the banker is not stimulated to lend.

I do not know if I have succeeded in clearing that up at all.

Mr. LUCE. If you do anything, sir, you demolish my whole understanding of the banking system. I had understood that the money with which a bank does business is secured from two sources, its capital, first, and secondly the money entrusted to it by the public.

Now, whatever the intricacies of the operations within the bank may be, I am still of the opinion that I put $10,000 at the command of the bank for its use, to make a profit. That is the way the bank lives, by the use of the money at its command.

Now, you spoke of the banks being glutted, and you went on to explain that, but I start with the understanding that the people of this country have put at the command of the banking system a much larger amount of money with which it can do business than it ordinarily has. That being so, I wish to know why we should put more money at the command of the banks.

Mr. ANGAS. I do not want to put more at the command of the banks in the sense of increasing their loan facilities.

Mr. LUCE. But, sir, this bill contemplates putting at the command of the banks an enormous amount of money which they do not now have.

Mr. GOLDSBOROUGH. Mr. Luce, that is your statement.

Mr. LUCE. I know it is my statement. I may be wrong.

Mr. ANGAS. What sort of money? Please explain the sense in which you use that word. Do you mean deposit money? You said that it puts at the command of the bank an enormous amount of money. The word has seven definitions. In which sense are you using it?

Mr. LUCE. I am using it in this sense. Today there is hardly in existence such a thing as interbank currency. But suppose that in a year the bank will have in its possession 100 million dollars of interbank currency. Therefore it will control the use of 100 million dollars of wealth that it did not before have.

Mr. ANGAS. Of money?

Mr. LUCE. Call it wealth, or whatever it is.

Mr. ANGAS. Monetary resources with value?

Mr. LUCE. Yes.

Mr. ANGAS. I am frightened at that word "wealth."

Yes; the bill does increase the reloanable resources of the bank, I agree.

Mr. LUCE. Now, why should we do that, when they already have an excess of value with which to do business?

Mr. ANGAS. End of question?

Mr. LUCE. End of question.

Mr. ANGAS. I agree entirely that this bill will increase the amount of reloanable monetary resources on the books of and under the control of the banks, but the purpose of this bill, as I see it, is not primarily to increase the amount of loanable money available to the public, assuming that it will want it, but to do something quite else, to increase the amount of money born very often through the process of loans under the modern credit system and increase the amount of money in the hands of consumers. An incidental feature of the procedure proposed in the bill is that simultaneously you put extra monetary purchasing power in the hands of consumers. The incidental feature is to simultaneously increase the loan facilities of the banks. I admit it; but the purpose of the bill is not to increase the amount of loanable facilities which are today huge, as I have already said, but to increase the amount in the hands of the people who can go into shops and spend, and/or, alternatively, to lower the prices that the consumers pay for each commodity, although it does not reduce the amount of money that retail sellers get for each commodity.

Mr. Luce. I can see that, sir, but——

Mr. Angas. I know that you have your finger very reasonably on one of the most difficult verbal subtleties of this bill and of the whole problem; I appreciate that. That is why I say I am so glad you asked that question. If anybody should wish me to clear up the mental confusion which widely exists on the technique of banking deposits, I will gladly do so now. I think it is imperative to do so in order to have an understanding of this bill, or any other bill.

Mr. Luce. Could I get through some general questions first?

Mr. Angas. Certainly, sir; I wish you would.

Mr. Luce. I want to go step by step into this.

You have recognized that this is an inflationary measure?

Mr. Angas. Immensely.

Mr. Luce. Immensely inflationary?

Mr. Angas. Full stop; immensely—full stop. But it has teeth in it to stop the inflation as soon as it shows signs of being dangerous. Otherwise it is a steering wheel, with immense powers to turn to the ditch of inflation on the right, and immense powers to put on the brakes and turn toward the deflation side when——

Mr. Ford. Would not "reflation" be a better word?

Mr. Angas. I love it; but I hate using gentlemanly words. [Laughter.]

Mr. Luce. Now, some years ago I read a carefully written article by, evidently, a capable economist, largely statistical in its nature, which seemed to demonstrate that inflation, unless of an abnormal variety, does not produce its effect for 2 years.

Mr. Angas. Bank credit inflation?

Mr. Luce. Any kind of inflation—that it has not produced its effect for 2 years. Only in very rare instances has it ever produced the effect inside of 1 year, and I will point out to you what happened in 1935. When the price index shifted, it did not shift appreciably for 2 years. That is, it was going up slowly, but there was no great increase inside of 2 years after the President, with his tremendous inflation program by the devaluation of the dollar, had set it to work. In other words, the price index, following the devaluation of the dollar, does not indicate that any inflationary measure, unless of the German variety or the French assignat, will accomplish its expected purpose for 2 years after its enactment.

If that is true, and the enactment of any of the scores of measures before the Congress be worth while, then the result will not be felt until 1940.

Mr. Angas. That question is remarkably clearly put.

I do not agree with the economist who says that inflation does not catch for 2 years. The speed with which any inflation catches depends on the mass psychology of the day. It is possible for the mere threat of inflation, sir, to speed up the velocity of money already in existence before it is inflated in quantity, that a very rapid price rise is produced before, not 2 years after, but before the actual inflation occurs.

An an example which refutes the economist in question, when Mr. Roosevelt made his Presidential address on March 4, 1933, to threaten money inflationary measures, in addition to going off gold, which in itself does not alter the quantity of money in actual circulation, the threat or anticipation, preferably, of that inflation caused an immense and gigantic price rise within 3½ months. There was confidence in the man. There was confidence in the Government. So that even a threatened change in the volume of money caused the price boom.

So the economist to whom you refer is wrong in that instant.

Later, in the same country, America, the inflation began, in quantity, very rapidly; as I said before, the inflation began very rapidly in 1934 and 1935, but money bills, like the tail end of the N. R. A. and other bills which frightened owners of money, led to an increased demand for money, paralleled roughly with the increasing supply, so that in that case the 2-year very gigantic inflation of net demand deposits did not catch.

There was, in fact, a 2-year lag until the war threat of last Christmas changed the psychology of the public concerning scarcity of commodities, or future demand for commodities, and then you got the gambling in commodities and the price rushed up 17½ percent in 2½ months.

That is why I say the speed with which an inflation catches depends on variations in public psychology, largely influenced by the press.

Mr. LUCE. That undoubtedly accounts for the zigzag in the line of the President's chart, put out last Friday; yet the general tendencies have been over a period long enough, I think myself, to warrant some general conclusions, and they seem to me to indicate the truth of the statement of the economist, statistical in its nature, based upon previous inflations, that inflations do not accomplish their purpose and go to work inside of 2 years.

Now, let us see the goal that this bill proposes, and you support it in your digest, except perhaps in certain details.

Mr. ANGAS. I am glad that you added that qualification.

Mr. LUCE. You set the limit, desirable limit, of 90 percent of 1926, and the President has taken that same position, last Friday, according to the newspaper men, but it happens that almost a year ago this week it was up to 90—that is, wholesale prices were. Do you think that we should do more than return to where we were a year ago today?

Mr. ANGAS. I doubt it. Within 10 percent of 1926, either on the over side or the under side, is about the range I think would be reasonably fair, in relation to the debt level.

Mr. LUCE. But the President pointed out what he did not recognize 4 years ago. He pointed out that these determinations work great injustice on persons who have made contracts. We argued that thing with all the emphasis we could on the floor of the House, but the majority of the House swept us off our feet, and the President ignored that which he would now follow.

How shall we meet his present attitude, that we should not injure persons who have made contracts?

Mr. ANGAS. It is a question of the happy medium to me. The ideal way of looking at the contract question is to see when most contracts were entered into, at what level of general purchasing power of the dollar, and if one could find that perfect point, that, from the point of view of contracts only, is the ideal point to go back to. That is the fairest. No statistician can make the perfect calculation. He can make rational guesses only.

I agree that altering the yardstick, namely, the dollar or the purchasing power of the dollar over commodities on the down side, which means a big rise in prices, is most unfair to all creditors, and should be avoided, it being in my view the duty of a government to provide its populace with the most stable yardstick possible. A perfect one is not possible, I admit.

Conversely, a huge shortening of the yardstick, or deflation of prices, is giving to all the creditors and persons with fixed incomes a fortuitous bonus.

In other words, whichever way you go, there is something wrong or unfair, either to people who entered into fixed money contracts a great many years ago or just a few days ago—is inevitable. There is an ideal figure conceivable in one's imagination, although, as I say, on the paper which you have before you it is not statistically measurable.

Mr. LUCE. Permit me to say, Major, that some years ago, believing that the 1926 level was near enough to be used, I championed it on the floor of the House, in support of the bill named after my good friend Mr. Goldsborough, and drew down on my head the savage denunciation of my own party leaders. So a burned child dreads the fire, and I am afraid to put my head in a noose again by supporting a measure which is now 12 years back.

Mr. ANGAS. I live with my head in a noose.

Mr. LUCE. It seems to me that we ought to forget 1926, in view of the truth of the President's statement as to contracts. If we forget 1926, why do you think we should have a higher starting point than we have today?

Mr. ANGAS. I rather agree about neglecting 1926. It is getting rather a long distance away, and a great many fixed money debts and charges have been incurred since 1926, and perhaps one's eye should be kept on the more recent years, rather than on 1926. That is why in that particular pamphlet I have not put my estimated reasonable price level about 1926, but rather below it.

Mr. LUCE. Now, to bring up another subject, you are familiar, I presume, with the writings of Foster and Catchings?

Mr. ANGAS. Most intimately. I regard it as one of the 10 great economic books in the world on the most difficult subject in economics, namely, balancing consumption to production. I know almost every word of it.

Mr. LUCE. I shall be glad to tell that to Mr. Foster, who is a constituent of mine.

Mr. ANGAS. Tell it to Catchings, also.

Mr. LUCE. The Foster and Catchings theory, as I grasp it, is that the production of the country only in part reaches the wage earner.

Mr. ANGAS. Excuse me; do you mean the money paid out in production, or the product, the things?

Mr. LUCE. The things.

Mr. ANGAS. Yes, sir.

Mr. LUCE. And that the production is divided between the wage earner and the employer, and, as the years progress, a point is reached where the wage earner can no longer buy current production. Do I state it accurately?

Mr. ANGAS. Yes, sir; absolutely.

Mr. LUCE. That being so, is the remedy to put more money directly in the hands of the wage-earner class by some form of distribution such as is here proposed, or is their remedy better, to expand money in good times?

Mr. ANGAS. Meaning by "their," who?

Mr. LUCE. Foster and Catchings.

Mr. GOLDSBOROUGH. You mean the remedy of the multitude, don't you?

Mr. ANGAS. I know what he means.

Mr. LUCE. I mean the remedy Foster and Catchings proposed is that in bad times we shall spend liberally, even lavishly, on non-productive enterprises. Is that reconcilable with this theory?

Mr. ANGAS. With the bill?

Mr. LUCE. With the bill, and many others of the same sort, because I am talking about various measures before the Congress, including the Townsend plan.

Mr. ANGAS. That is the great merit of this bill, and, as I said in my opening remarks—"When this bill was first sent to me, I glanced through it quickly and put it to one side, rather expecting it to be of a character similar to so many other intended cures for trade slumps, and I expected it to contain numerous fallacies in relation to how the trade cycle may be cured. When I had time to study it more carefully, which I did, I found that it contained what appeared to me to be a very practical method of dealing not only with this slump, but with slumps in general."

This bill is not necessary for this slump. I can cure this slump in a day. I reassert that, that I can cure it in a day, if I were in a certain position.

This bill is important, not for this slump, but for another type of slump which can occur for other reasons. This is a psychology slump to me. This bill is important on those occasions which are analyzed by Foster and Catchings, and that is where the bill appeals to me, not in all its features, but in its main features, and I will say further that this bill will work at the center. There is no difficulty at the central banking system. It does not involve a change in the existing system. The details of administration on the outer circumference in the congressional districts I am not so certain about. I do not say it won't work. I do not say it will.

But I am so glad, sir—in fact, I am surprised, sir, that you have raised that point, because that is the dominant feature of this bill compared with numerous other schemes which I have read, and I was going to later on show that that is where this bill contains a real germ of sense.

When I first picked it up, I said that this was another crazy inflationary bill, one of these social-credit schemes which I have discussed with some of the people whose names are well known, bristling with monetary nonsense. I was surprised to see that this bill had actually seen the snags, seen the disease and seen the normal snags and the remedies. I was astonished. So I did come down here to give evidence. I do not support the whole of the bill. I do not condemn the whole of the bill.

Mr. LUCE. I do not think I made myself clear. Your answer is evidently——

Mr. ANGAS. It is drifting.

Mr. GOLDSBOROUGH. It sounded pretty good to me. Why can't we let him finish.

Mr. Angas. You misquoted Foster and Catchings, sir. You said that their remedy was government works, spending on the consumer side of a nonproductive nature.

Mr. Luce. Yes.

Mr. Angas. But that is only one of their remedies, and at the end of each of their tables they say, "Unless more money is added on the consumer side."

It is not quite an accurate quotation of Foster and Catchings.

Mr. Luce. I am glad you explained that, but the point that I wish to bring out is that Foster and Catchings say that too much is being produced, and therefore lessen production. Now, Mr. Goldsborough says too much is being produced, therefore add to production.

Mr. Goldsborough. I do not agree that I made any such statement as that, either in the bill or in writing.

Mr. Luce. I will withdraw it then.

Mr. Angas. He nearly says it, but he merely says, add to money so as to afterward add to production.

Mr. Luce. I am emphasizing merely the view, if I understand them aright, that they wish to reduce for the time being the production of consumers' goods.

Mr. Angas. No, sir; not as I understand their books.

Mr. Luce. I thought that their theory was based upon that assumption.

Mr. Angas. No, sir. They say it must be done unless one of their cures is adopted.

Mr. Luce. Let us go on and see where we come out, omitting those exceptions. They start with the principle that the mills and the factories are producing more goods than the consumers can use, because they have not the purchasing power.

Mr. Angas. I agree.

Mr. Luce. We are asked to pass a bill which will continue the purchasing power and perhaps add to the power of buying consumers' goods.

Mr. Angas. Yes, sir.

Mr. Luce. Therefore there seems to be a contradiction between the two theories which cannot be reconciled. If Foster and Catchings are right, and we are producing more than the consumers will buy, the remedy does not seem to me to put it within the power of the consumer to buy more.

Mr. Angas. I think that is precisely what it does do, this bill, and that is precisely the cure mentioned by Foster and Catchings. Otherwise one has to reduce production, sir, to make the world healthy again, as I discussed yesterday. May I reconcile the verbal problem?

Mr. Luce. Yes, go ahead.

Mr. Angas. And the question of what starts up the machine again and what makes the wheels go round.

I will preface this. This bill is a branch of managed money. It is not the whole theory of money. It is, if you like, a hat put on the existing methods of managing money, an additional hat, a top hat. The interesting part of it to me is that it knows where to inject money into public circulation. The present system of injecting money, which is, as you say, bank loan money, and therefore born for the most part with loans and investments by the bank—the wrong thing is the form of injection, and that channel of injection is that money goes into active circulation in the course of producing more goods, in the productive side, as a general rule. This bill injects it into circulation on the consumer's side.

Let me give you an illustration. Walk outside your hotel, or whereever you live in Washington, and go into the retail shop opposite on some crowded street. You will say to the retailer today, "How is trade?" He will say, "Atrocious." You will say, "Why?" He will say, "The public won't buy."

Go out of the shop again onto the sidewalk, and ask an unemployed man, "Why don't you go and buy in that retail shop? They want to sell." He says, "I have not got any money." You say, "Why haven't you got any money? There is plenty of money in the country. The banks are bristling with it." He says, "I haven't a job. I cannot earn any. I have been all over the place looking for a job."

Then you go over to the manufacturer and you say, "There is a man out in the street. Why don't you give him a job? It is your social duty to give him a job." He says, "I would love to, but it means increasing production, and I have already a big inventory and I cannot sell what I have already produced. That is why I don't give him a job." You say, "Why can't you sell what you have already produced?" He says, "The wholesaler and the retailer have too much already. They cannot sell it."

So you complete the circle of visits and inquiries, and find that in the midst of plenty the situation is crazy, and it would need only one good brain to clear it up, but he must have the power and an audience.

This bill will clear that problem up. Any bill which injects money to consumers, to those men on the sidewalk, which enables them to go into the retail shop and reduce the inventory so much, will result in the retailer giving an order to the manufacturer when his inventories have fallen, and that will make the manufacturer once more start paying incomes out to the man on the sidewalk, but under the present money system, the distributive system, money, as it happens, does not get injected into circulation except to people who enlarge inventories, middlemen, in fact, or to manufacturers who produce more goods, properly speaking.

Mr. TRANSUE. That is the way to increase confidence?

Mr. ANGAS. I am just stating the circuit flow of money. I do not see the relevancy of your question. Perhaps I did not hear it.

Mr. TRANSUE. My question is that that is the way to increase confidence. You mentioned a little while ago that we were in this slump because there was not confidence, and I am asking you if you pointed out the way to increase confidence.

Mr. ANGAS. Confidence, you see, has five definitions. Read one of the last chapters of my pamphlet, "Remaking the Boom." Anything which will improve the circuit flow of money and make trade better will increase the confidence of businessmen. The whole thing, looking at it, has appeals. As things are working today, it is deplorable. A cure obviously is possible, and the thing to do is to find a cure which does not create even greater diseases, like the German inflation, or something which spoils the moral fiber of the working portion of the Nation, like my moral fiber has been spoiled by living many years on the earnings of the banking system without doing any work for pay.

Let me enlarge on this, please, if I am of any use to you at all. Such a cure has not been invented by any country in the world. Therefore the cure to the obvious dilemma, anomaly, must be subtle in terms of verbiology; it must be confusing, and I invite you to read through the evidence of this committee for an appreciation of the confusion of words and of bookkeeping terms which can occur in the Banking and Currency Committee of the leading industrial nation of the world. I say that without insult. It is the language of the subject with which we are dealing.

It occurs in my country, and France, and Germany, in the case of Mr. Havenstein, the chairman of the Deutschbank, as to whom I recited to you a story day before yesterday. It is difficult—and this is why we are not wasting our time, nor is the committee—every cure that is suggested has some bad points—every cure. The actual cure will have a case against it, and will have a debit as well as a credit side in terms of good and bad points.

I hate that word "credit." It is something which has puzzled the best brains of the world, because it involves watching something moving in a flow which it is difficult to treat on paper as a static fact. It requires a mind that can see happenings in motion, and yet can be clever enough to write about them on static paper. Foster and Catchings have approached it. That is why I say it is one of the great books.

Now, to solve this problem—and I am not off the point. You think I am, probably, but I am not. The bill provides it. I do not say that it is a very just distribution of wealth to give the relatively poor on the streets, who are apparently not at the moment of great economic use to the Nation—they are alive, but they are not producing anything or being used, and I do not know whether you regard it as fair or unfair to inject money among those people, but the point is that if you do, you speed up the wheels of industry, and get confidence. If you go on doing it too much, it becomes overeating, because when confidence has returned you get your flow of money stimulated again, and you will get wild prices back, and I assure you that if this bill is adopted, or any bill with its features, in the next few months, during this slump, where there is a lot of hoarded money, you will get a very sudden price inflation in the grand manner, probably as sharp as in 1933, when the President threatened to inflate, and as soon as such a bill was applied, you would have to cancel the discount, because all of this enormous hoarded amount of bank money would revelocitate again quickly. It would give the thing a kick, like kicking a snowball over a precipice in Switzerland.

That is all that is wanted in this country today, and that is why I said that, if given a certain position in this country, I could cure the slump, and what I would do is this: I would do it with words. Words can cure the slump, because words can recreate psychology, I think. I would merely say, if I were king, "Profits are too low in this country. That is why business is not giving jobs to men." Profits are falling. I want to see profits go up. I know it is the key to the capitalist system.

I would, secondly, say that prices in my view are too low for the fixed charges. Net realized prices are too low, about 12 percent. I want to see prices up, the general price level. Some, I know, will go too high. It might be that some commodities would lag behind too much to my liking, maybe agriculture, and maybe cement and some others would go too high, but I want to see the general price level up, and in order to do it I would do something to get it up. I would go on injecting the supply of money until I were to frighten those who are speculating in money, so that bulls of money turn into bears, and the velocity of money increases instead of decreases, and the result will be that confidence in money would diminish and you would get your circuit flow going again. I will guarantee it, although I do not want to give the impression that this bill is necessary or the only cure for this slump.

Mr. GIFFORD. "If I were king," you said.

Mr. ANGAS. Yes.

Mr. GIFFORD. Have we one, or is there a possibility of having one?

Mr. ANGAS. A king, or monarch, or leader.

Mr. GIFFORD. You said that if you were king, you would do that.

Mr. GOLDSBOROUGH. That is a political question.

Mr. GIFFORD. I can ask it.

Mr. ANGAS. I said that if I were king, with power, I would do that. If you like, I will say, if I were fuehrer, with power, or if I were dictator, or if I were prime minister.

Mr. PATMAN. Or the Chairman of the Federal Reserve Board?

Mr. ANGAS. Maybe, but there are people whose voices are listened to with greater attention.

Mr. GIFFORD. Could you do this if you were President?

Mr. ANGAS. If I were King.

Mr. LUCE. To round up my own questioning, Major, I would like to say that I still find it hard to accept any remedy for this situation which puts purchasing power in the hands of people who have not earned it.

That is all.

Mr. PATMAN. I would like to ask some questions.

You either misunderstood Mr. Luce, or I misunderstood Mr. Luce, or I do not understand your testimony. A while ago Mr. Luce asked you the question about the quantity of money, and if I understood your answer correctly, you said that it did not amount to anything, the quantity of money. I think, though, you must have meant the quantity of actual physical tangible money as distinguished from bank credit. Am I correct in that, or did you really mean that the quantity of money, meaning tangible money, bank credit and all, did not have any value in connection with solving this problem?

Mr. ANGAS. It is difficult to remember verbatim your question. My answer is, as regards the subject matter, that changing the total volume of money, or even threatening to, will ginger up velocity, and therefore it is a potent, ameliorative factor.

Mr. PATMAN. That is the way I understand your testimony, but I did not understand your answer to Mr. Luce's question as being in accordance with that.

Mr. ANGAS. I must apologize for being vague.

Mr. PATMAN. Possibly I misunderstood it.

Awhile ago you mentioned the interbank currency as being inflationary. If I understand this bill correctly, a 100-percent reserve is contemplated. If a 100-percent reserve goes into effect, and I as a retailer have made a sale to you on a purchase amounting to $100, I will take the maximum of $85 to the bank, and I will receive the other

$15 from the bank, and that $15 is, so far as the bank is concerned, interbank currency, and a 100-percent reserve must be maintained against any loans on this interbank currency.

Mr. ANGAS. Do not call it loans.

Mr. PATMAN. Now, the point is that if I as a merchant receive credit for that $15, that bank owes me $15 and it has to keep that interbank currency as a reserve against it, but can the bank make a loan of that to anybody else and keep a 100-percent reserve?

Mr. ANGAS. The answer is, it cannot.

Mr. PATMAN. Therefore it would not be inflationary, would it?

Mr. ANGAS. Yes.

Mr. PATMAN. So far as bank deposits are concerned?

Mr. ANGAS. No—one minute.

Mr. GOLDSBOROUGH. I think that there is a misunderstanding. Unless you do not want me to, I can correct you on the bill.

Mr. ANGAS. I do not want you to. I understand the question, and if I might, I would like to answer it. Otherwise I will have two questions, or three or four, all at once.

Mr. GOLDSBOROUGH. Interbank currency is not eligible as reserves.

Mr. ANGAS. He did not say it was. He said there was a reserve of interbank currency.

Mr. GOLDSBOROUGH. I understood him to say there is a 100 percent reserve, and I say that it is not held as reserve at all. It is just a deposit.

Mr. ANGAS. I do not like the wording in that section of the bill, not that it is any different in reality; it is merely terminology. I do not happen to like the word "deposit" for a reserve.

Mr. GOLDSBOROUGH. It is not a reserve.

Mr. ANGAS. I do not think it alters the reality. Mr. Patman used the word reserve. I understand what he means, to make that for the new bank credit, deposit currency, created by the member banks. There is 100 percent backing for that deposit; that is true, and then he asked me why such action was not inflationary. He did not say whether he meant the total deposits on the bank's books. The total bank deposits would go up under this bill, certainly, parallel with the interbank currency.

Mr. PATMAN. No question about that?

Mr. ANGAS. No question about that.

Mr. PATMAN. But, so far as being used as a basis for other loans, it would not be inflationary at all, because it could not be used.

Mr. ANGAS. No, sir. That extra deposit would not be inflationary of the quantity of money—I did not say of the price level—a second time. When it is created the first time, it is inflationary, but it is not a basis for a second superimposed inflation, I think.

Mr. PATMAN. How would you keep that separate from your regular bank reserves?

Mr. ANGAS. You could keep it separate on your books if you wanted to. Actually there would be no necessity, because under a cash reserve ratio system—fractional reserve system, you call it—there can only be additional loans or investments made by your bank if it has sufficient reserves, excess reserves, and it is always willing to rediscount paper at the Reserve bank.

Mr. PATMAN. Would there be danger of a bank accumulating so much of the interbank currency that it would displace the other currency or reserves in that bank to the extent that the bank would not be permitted to make a sufficient profit or do sufficient business?

Mr. ANGAS. That is a very subtle question, and I will give you an equally subtle answer, using "subtlety" as mental subtlety as distinct from subtlety of character.

This bill, if adopted and kept in existence for many years, will gradually, in my view, eliminate the fractional reserve system or cash reserve system of banking. I will explain why in a minute, if you wish. It will therefore tend toward what is now popularly called 100 percent money 50 years hence or 5 years hence, if you like, when the volume of trade done by America is five times as great and the standard of living of the poor ten times as great—maybe. You would have most of your bank deposits appearing on the books, say, of the Chase National Bank, backed 100 percent by these interbank currency notes, and only a very small proportion of the remaining deposits appearing on the Chase National Bank's books, and if you could separate them, which you could not very easily do, according to the present method of accountancy, only a very small proportion would be on the ratio of 26 percent, it being a bank in a reserve center.

Mr. PATMAN. New York or Chicago?

Mr. ANGAS. Right.

Mr. PATMAN. Have you finished?

Mr. ANGAS. I told you the answer. You said profits. That is why I said the question is mentally subtle.

Mr. PATMAN. I will withdraw that part of it.

Mr. GOLDSBOROUGH. We are interested in that, or I am, and I would like to have him answer that part, because that is a very important part.

Mr. PATMAN. Go ahead, as to what effect this would have on the profits of an institution.

Mr. ANGAS. At present the banks are performing a service to the check-using community for virtually nothing, a very expensive service, the keeping of one's private accounts and handling one's checks if one keeps a few thousand dollars or even less in the bank. On that they tend to lose. Not necessarily do they lose, but it tends to be more expensive, and since it is a service to the depositor, if he kept no balance it would obviously be something given for nothing, which would be uneconomical. If you and I kept an idle balance of only about one dollar, and had transactions through a check book running into many millions, the bank would be giving us a service and for such a service it would be reasonable for them to charge. They are running that particular part of their service in many cases at a loss, and in other cases certainly they will hold very large idle balances on which they realize and on which therefore they make a profit, so it cancels itself out, in a way.

But let me interject a further general thought here. The banks, in an expanding country, if they can get extra reserves, getting extra loan facilities, which this committee has been referring to as 10 to 1—I won't argue the fractional ratio—have the power to create credit out of nothing by means of a loan or investment, and that is using the word in the term of bank credit money which circulates, and they get paid perpetually interest on the loans and may be interest on the investments, unless the investments default, so that on every dollar these banks create out of nothing they get interest per annum perpetually, as long as the deposits, so-called, which are created by the loans and investments do not shrink.

To give an example, the present Administration in this country has borrowed 8 billions from the banks, I believe the figure is, since the slump, at about 3-percent interest. They are paying somewhere around 200 to 400 million dollars a year to the banks' shareholders, because the banks' shareholders own the money factory, which, although not legal tender, is used as legal tender and goes current. It looks very unfair. Theoretically it is, although the Angas family made a lot of money out of it, I admit.

But the excuse for this anomaly going on is that the banks are doing something for nothing, for about 90 percent of the money transactions of the country so that is an alleviating excuse for the banks being allowed to continue possessing this facility.

On the question of profit, this bill does not say that the banks, if they received gold from abroad or legal tender issued to them by some central authority, the subtreasury, in the form of gold or gold certificates or silver—this bill does not say that the banks shall not go on lending on any cash that they get from the factories or the mines or even from public circulation. It does not say that. So it does not necessarily hit the profits of the banks and send them down, but it does take away, probably, their future capacity for earning perpetual interest on any additional bank deposit money that goes permanently into future circulation, and that is the answer to the second half of the question concerning profits.

Mr. PATMAN. In other words, the difference in the amount of money that the banks have as a basis for these loans and the amount of the loans?

Mr. ANGAS. Which loans?

Mr. PATMAN. I mean all loans.

Mr. ANGAS. May I interrupt you?

Mr. PATMAN. Loans and investments.

Mr. ANGAS. All right.

Mr. PATMAN. Which I presume could be designated as the Nation's credit. Would that be a phrase that could properly be used there? In other words, the difference in the reserves they have and the amount of loans they have made is really the Nation's credit, and therefore you contend that that should be used in the interest of the public, and those who use the banks should support them by paying adequate service charges? Am I correct about that?

Mr. ANGAS. Yes, although the words "social credit" are like a red rag to a bull.

Mr. PATMAN. I mean the Nation's credit. It was a vague phrase—I admit that.

Mr. ANGAS. It is like a red rag to a bull, to me, because it is so vague.

Mr. PATMAN. I am in accord with what you say there.

Mr. ANGAS. I do not like the word "credit." I am always disagreeing with you about your use of the word "credit."

Mr. PATMAN. I know I am very careless in the use of words.

Mr. ANGAS. We are all careless in the use of words. It is not exactly the Nation's credit. It is the Nation's law which says that something shall be legal tender.

Mr. PATMAN. I agree with you that prices are not high enough, considering fixed charges, and that the general objective of this bill is desirable, to place purchasing power in the hands of the masses. The gentleman realizes, however, that this will give just as much additional purchasing power to one who does not need it as to one who does need it?

Mr. ANGAS. I agree.

Mr. PATMAN. And that two-thirds of the people already are in position to buy the comforts and necessities of life?

Mr. ANGAS. Yes, sir.

Mr. PATMAN. It is only the one-third that represents the class that the gentleman mentioned awhile ago.

Mr. ANGAS. And the unemployed won't get it.

Mr. PATMAN. Those that are walking by the store?

Mr. ANGAS. At the first injection they won't get it.

Mr. PATMAN. Does the gentleman believe, if you want to use what I called awhile ago the Nation's credit, using a loose phrase—if we want to use the Nation's credit in that sense; that the most desirable way would be gradually and eventually to retire the national debt and save the people almost a billion dollars a year in interest?

Mr. GOLDSBOROUGH. Now, Mr. Patman——

Mr. PATMAN. That is a completely separate subject.

Mr. GOLDSBOROUGH. It happens that I have to go, and I have engagements for all afternoon.

Mr. PATMAN. I just have two or three questions.

Mr. GOLDSBOROUGH. Suppose that we adjourn until half past 10.

Mr. ANGAS. May I answer Mr. Patman's very reasonable question, if you will allow me a minute or so? He asked me a question if another system would not do the trick. That is a fair question.

Mr. PATMAN. Would it not be a more desirable use of the Nation's credit?

Mr. ANGAS. If I were to give you my methods as to what I think more desirable, it would take hours. As to whether there is any improvement on this bill or amendments to it, or whether the existing system could not do the same thing without the bill, I can conceive of many such methods. I admit it. This is not the only thing in the world which will do the trick.

Mr. FORD. I just wanted to ask one question, and to show you a table, if you will think about it. I have here a statement from the Federal Reserve, showing the total loans and investments in the banks of the United States, Federal banks of the United States, and they amount to $31,750,000,000. The total deposits amount to $40,000,000,000. The total reserves are $7,050,000,000. The required reserves are $5,800,000,000; excess reserves, $1,200,000,000.

On the basis of that calculation, the banks could now loan $8,300,000,000 more than they have.

Just look those figures over, and tomorrow I will want to ask you a question in connection with them.

Mr. GOLDSBOROUGH. Gentlemen, without objection, the committee will adjourn until half past 10 tomorrow.

Mr. FORD. It is a monetary question.

(Thereupon, at 12:30 p. m., an adjournment was taken until Thursday morning, February 24, 1938, at 10:30.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, FEBRUARY 24, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on H. R. 7188 were resumed at 10:45 a. m., Hon. T. Alan Goldsborough presiding.

Other members of the committee present: Mr. Reilly; Mr. Williams, Mr. Spence, Mr. Ford, Mr. Brown, Mr. Patman, Mr. McKeough, Mr. Transue, and Mr. Luce.

Mr. Goldsborough. The committee will be in order.

Major Angas told me this morning that he had a connected statement he would like to make without any interruption whatever. Of course, when he is asked a question, he does not like to hold up an answer, but he would like to make this statement without interruption if the committee is agreeable to it.

Now, Major Angas, will you please proceed in your own way?

STATEMENT OF MAJ. L. L. B. ANGAS—Resumed

Mr. Angas. I will not take more than 10 minutes.

So far I have been talking around the bill, rather than on the bill. I see in the newspapers again that I have been talking for the bill. It is not true. I have said nothing for the bill. I have said some things for certain parts of the bill. If I am to be at all useful to the committee, I will discuss the principles of the bill, rather than the details, which it is not for a foreigner to discuss. I have been trying to do that, but so far I have said nothing about four or five points which enter into the bill or into the philosophy of the bill, namely, first, Is money wealth? Secondly, Is increasing the volume of money increasing the volume of wealth, or is the money of a country worth so much in terms of commodities, regardless of the number of units that you print or write with a pen in a bank's ledger?

I have said nothing as to whether time deposits are or are not money. In my view, they are not, although there is a border line respecting a quantity of time deposits which are practically the same as demand deposits. I have said nothing whether the backing for currency, whether of gold, silver, or legal-tender notes, governs its value. On the whole, it does not, but has a mild psychological influence, but it is comparatively unimportant in determining price level, whether you have a backing like you have in this country, of gold, roughly, 100 percent or 200 percent of the value of the notes outstanding, or whether, as in Germany, the backing is only 3 percent. I have said nothing about that, nor do I propose to, unless asked.

I have said nothing about the problems of foreign exchanges. I have not explained how essential it is to have a money system where money can be injected not only on the producer side of industry, as is customary now, under the loan method of making money or manufacturing money. I began to do so yesterday, but the sequence of events diverted me from that discussion.

I also said nothing about the art of keeping money expanding parallel with trade. I have only discussed keeping money expanding parallel with fear, and the increasing liquidity demand of money. I have not discussed the complex problem of increasing it parallel with trade values, like in 1928 and 1929, when there was no fear. I have also not discussed the problem of the two sorts of money, legal tender and bank credit. It is not enough merely to increase bank-credit money parallel with trade, but there should be in the currency system some arrangement to increase the legal tender also.

We use two moneys in the Anglo-Saxon countries, and the problem of money management is not creating only gold, or only notes, or only bank credit, but of having a parallel creation or injection of the two, a difficult problem. This bill does not deal with that.

I have also not said anything about where to inject new money. This bill goes very much to the heart of the place at which to inject it, in that circuit flow of money which I was describing yesterday when discussing the shop that could not sell and the unemployed man who could not buy, and the employer who could not employ the unemployed man, because the inventories of the retailers were already too big.

I have not discussed the problem of where to break the vicious circle, nor have I discussed the very complex and important problem of withdrawing money from circulation after it begins to show an inflationary effect. This bill is excellent on that point, in my view. So many of the bills suggesting cures which I have read are ridiculous. They see the importance at times of inflating both bank-credit money and legal-tender money, but they nearly always omit the vitally important factor of being able to withdraw it when the initial injection has so stimulated the velocity of our money already there that you get a price-inflation result which affects also the purchasing power of money. It is most important.

One must remember that money is not merely a medium of exchange, but also a measure of value, and one cannot have the dollar or pound dancing all over the place in purchasing power.

In the last 6 months, the yardstick of value in America has shortened 12 percent; that is the fall in prices that any index shows. The result is that every creditor is 12 percent better off, assuming that he gets his debts paid, and every debtor is 12 percent worse off. It is fantastic, letting the yardstick jump about like that. It is almost as ridiculous as letting the yardstick jump in the opposite direction, as happened in Germany in 1920. It leads to political rows and great unfairness, and it is puerile, in my view, not to have a system of money aimed at keeping the yardstick stable in purchasing power. The gold system does not do it, and did not do it. That is the point that I have not at all discussed at any length.

I have also not discussed the problem of saving in the modern capitalist state, a very difficult problem. The honorable member on my right, Mr. Luce, raised the point—I am very glad he did—of the difficulty which is analyzed so ably by Mr. Foster and Mr. Catchings in their book, Profits. In that book, in which I admit there is room for improvement, the authors drew attention to the fact that if a consumer who had just received money for producing goods did not spend it on goods himself at retail, but lent the money to some new producer, a dilemma began to rise, namely, that the producer also paid out that money to the consuming public again in the course of producing a second batch of goods, with the result that another batch of goods came into existence and on offer at retail so that you got one lot of money out of the two lots of goods on offer.

Everybody knows that savings are desirable for capital expansion, and to try to prevent saving for capital expansion would be mere foolishness, but just as there can be expenditure of money twice in succession on the consumption side, which I will shortly explain, so there can be expenditure of money twice in succession on the production side. Look at the way inventories get cleared during a slump, like the present moment, how they fall. It is as the result of money being spent twice in succession on the consumption side.

Take, for example, a retail shop whose inventory is too big. It wants to reduce that inventory, and so it does not give any more orders to producers, and therefore producers do not pay out any more incomes to the consuming public, so that the consuming public cannot buy. It is the dilemma of the whole thing becoming frozen up, but time goes on and effects a cure. That is how all past trade cycles get cured.

What happens is this: The public who have money go into the shops and buy commodities, and then the shop owner, instead of passing the money on to a producer and replacing the inventory, keeps it idle, but he has a wage bill and overhead charges to continue meeting, so without giving a new order to the producer, he pays his salaries again next week, and his rent, and that puts the money into consumer circulation again, and then the consumers go into the shop the second time and take goods out of inventory. That reduces the inventory a little bit. Then the shop, again meeting its overhead charges, once again pays out that same money into the general public, who again can spend it in the shops, and that is how inventories eventually get cleared. It means that production stops the whole time, but that is the way inventories get cleared, and if the retailer will take a loss at the same time, as Mr. Catchings so ably explained, and if he will sell goods for $50 that he paid $100 for, the money paid out to the public in producing those goods at, say, about $100, only $50 of it will be required to clear that quantity of goods, so that there is another $50 left for buying a second lot of goods. Very complex.

That is another technical method in the circuit flow of money, as to how inventories fall. That is the way inventories get reduced after they get to a level considered too big. The manner in which they can get too big is because of saving. Inventories, if there were no saving, should not get very big, or ever too big, because if you get all employers trying to double their inventories, the procedure is as follows:

They give orders to manufacturers, who then pay out money to the public in the course of production, which gives the consumer or the public enough money suddenly to buy the goods that are soon going to be placed on offer by the retailer at a price equaling cost. I admit there is something missing on the profit margin point, which Mr.

Catchings has analyzed most ably. To attempt to increase inventories is not likely to succeed, except under certain conditions, because, taking the country as a whole, the retailer who tries to increase his inventories gives his orders to the producer, who gives the public money during the course of production which makes them spend in the shops, probably, before the new production required for the extra inventory is completed, so that, broadly speaking, an attempt to increase inventories leads to a decrease, because as income is increased among the public, consumption increases. But if there is saving by the public, as I said earlier, who get money out of production, and they lend it back to producers to produce an extra lot of goods, you do not get the consumption which might be called normal, that completed circuit flow. Of course, the same money one lent to the producer is paid out by the producer to the consuming public; of course it is, and they buy one lot of good, but in the meantime a second lot of goods has been produced.

Now, I cannot in 5 minutes go into the very complex problem which Mr. Catchings took 260 pages to describe, but the point is this about this bill, and I do not think the authors of this bill appreciate it, because reading all the evidence presented both in print and in typewriting, they have never made the theoretical case for their bill which is really the strong point of the bill, namely, that it injects money on the consumer side.

Mr. GOLDSBOROUGH. You say we never made out a case for that?

Mr. ANGAS. I do not think nearly as well as it can be made out.

Mr. GOLDSBOROUGH. You have not read the evidence.

Mr. ANGAS. The system is so——

Mr. GOLDSBOROUGH. I talk about it in my sleep.

Mr. ANGAS. I have read every word, and I do not think a good enough case has been made on that score.

Mr. GOLDSBOROUGH. I am sure that you could improve it, and I wish you would do it.

Mr. PATMAN. I wish that you would discuss the administrative features of the bill. I am not concerned about the objective. I am for the objective.

Mr. GOLDSBOROUGH. Mr. Patman, I made the statement before you came in that Major Angas had requested that he be allowed to complete a short statement that he wanted to make before questions were asked him.

Mr. PATMAN. I had not finished questioning him yesterday, and I thought that you were going to permit me to resume this morning.

Mr. ANGAS. May I be polite to the bill and rude to the bill, but I do not want to be reported as giving evidence for the bill, but on the bill. I am not that impertinent Englishman who is trying to get a bill through, nor kill a bill in America.

In my view, the bill is technically sound at the center, within the banking system, technically sound, and, given scrupulously honest bankers, it will work as regards the center. I will discuss the administration, if I may, as I see it, at what I call the circumference, out in the country, later.

The bill provides a method of inflating money on the consumers' side of industry which no other bill that I have ever read does so well, at the same time as it arranges for withdrawing that money when it gets dangerous. This bill enables money in general, bank deposits, to be contracted when cycles of price inflation occur.

The method adopted, I admit, is to retire not the inter-bank currency notes, but to squeeze out of existence bank money issued against other reserves than interbank currency, which thus gradually, as I said yesterday, eliminates the fractional reserve system of banking. It eliminates pyramiding.

In my view, since the fractional reserve ratio system of banking has so many natural diseases in it—nobody's fault; I discussed that the first day in my evidence, and I won't repeat it now—the gradual elimination of fractional banking to me is not objectionable. I do not say it is urgent and necessary, particularly when a country is off the gold standard.

On the gold standard it is a terrible system, which I have analyzed very carefully in my book called The Problems of the Foreign Exchanges. I rather like that feature of the bill, of gradually eliminating fractional reserve banking, because it is in ratio reserve banking that one gets these huge swings up and huge swings down, and when bank reserves get strained, you get such a terrible tug, like they got in my country in 1919 and 1928, that the house of cards falls down with a complete flop.

That I won't enlarge more. Perhaps I may be asked something about it later.

There is, in the center, room for cheating in this bill by a not too scrupulous banker. This is the chief flaw at the center of the bill. It is fairly unimportant, but there is room.

The bill says that in event of a bank suffering a run on itself for cash, that the banker can apply to the—did you say the Secretary of the Treasury, or who was it?

Mr. PATMAN. The Federal Credit Commission.

Mr. ANGAS. The Federal Credit Commission, I think, or the authority—somebody. Help me with the name, please.

Mr. WILLIAMS. Federal Credit Commission.

Mr. ANGAS. Right. The banker may apply to get cash against the interbank currency notes. That is a very excellent provision, but it is difficult for me to define what a run on a bank is. What is the difference between a strong run, due to loss of confidence in that bank, because probably the officers of it have been foolish bankers—what is the difference between a strong run, and a mild run, or a weak run?

If I were a banker and wanted to defeat social welfare, for the benefit of my own profit, and if I were a small banker, and happened to have one rich man as a client, who normally left a million dollars in my bank idle, I might do this: I might say, "You are a good friend of mine. I wish you would take that million dollars out in cash and keep it until I tell you, because then I can go to the Federal Credit Commissioner and say there is a run on my bank; please convert my interbank currency notes into cash, and then for quite a long while I might pyramid on that."

I won't enlarge that. I know there is an answer to it, but that is one method of a single banker cheating and enlarging his own reserves on which he can build further deposits by a trick.

As I said, on what I call the center of the circle of administration, on the bill as regards central administration, I admire its ingenuity.

I regard it as practicable. I do not think it upsets the existing banking system. It is not one of those revolutionary changes which never works. It is not, in fact, like many of the other panaceas for the money problem that one has the misery to read year after year in all countries.

But I am not a person to say that a bill must be good just because on the whole it is theoretically sound. A bill, in the real world, to be useful to society, must be practically administrable, and here there are some features of the bill which appear to me, as a foreigner, unworkable.

Now, I said yesterday that just as members of this committee might hesitate to go down to Peru and lay down the law as to what would work in Peru, so do I hesitate to say what will work in America in respect of this bill, but you have honored me by asking me to give evidence on the bill, so I presume it my duty not only to press the majority of its features as regards the central administration, although I have condemned two points, but also to analyze, so far as I am able to, what seemed to me to be the obvious defects, despite the many merits, on the circumference, and I have emphasized those merits more by implication, on the assumption that you have studied the Catchings theory, instead of spending 5 hours in reading through his book aloud, and I am sure that this committee has made a study of that problem, since it has been sitting so long, and if I may add, sir—if I may honestly add, sir, now that America is far and away the leading industrial and financial country in the world, I rather look to this committee of a few men only to produce the solution of running the capitalist system properly, in a conservative way.

Forgive the aside, but I would like to express this view. Here is a committee at the center of the economic and financial world, which is bothering to sit and listen to me and others who are anxious to improve things, and out of this committee some day will come the cure, I hope, to this dilemma of plenty causing what?

Forgive that, sir, but I am very sincere on that point. I think this is the center from which might come a clear understanding of the capitalist system and the socialist system, and perhaps the solution of the faults of capitalism.

On the circumference of the circle, my first objection to certain clauses of the bill is that the problem of definition is so difficult—I have already said it is difficult to define a run on a bank. To me it is difficult to define what retail trade is. I write books myself, and certainly a book store would come under the heading of "retailer." I am sure that that is not disputable. How, then, if I sell my own book? The question is, am I not a retailer? I do not think that you can define the retailer.

I might enlarge upon this by examples much more, but that is the objection. I do not think that you can define a retailer. You may be able to define a natural person—probably, yes. But I do not see that you are able to prevent a natural person, if successfully defined, from interposing between a manufacturer or a corporation, as in some of the evidence that was referred to. The question was, could Mr. Ford buy a locomotive through an agent, and the agent get a commission. I need not go on. You heard the evidence. It is all down on paper.

That is another fault. Even if you succeed in defining a natural person, I am not sure that you can defeat certain details of the bill by the interposition of somebody who will cheat.

Another objection is that if the discount being given was very high, say, 15 percent, there is scope in those few trades where the profit margin above cost is less than 15 percent, say 5, for a tricky intermediary to get in and do what is called an arbitrage operation. Perhaps I need not expand on that, but if the profit at which things are sold is only 5 percent, and the discount is 15 percent, there is room for three turns of 5 percent.

Mr. **Ford**. You call that chiseling.

Mr. **Angas**. Chiseling; yes. In the London foreign exchange market they call it arbitrage—a pretty word. There is scope there.

Then the retailer might, on the institution of this bill, mark up the prices of his articles 15 percent. With things like bars of chocolate, which have a fairly fixed price, it is rather impossible, but with things like a glass ash tray, he can stick any price tag on that he likes, and since there is a great deal of lethargy among the clients of any given shop, particularly in little villages, he might succeed in marking up—I do not say his old stock so much, but any new stock, by something like 15 percent, so that the bill would become a bonus to retailers.

It is true that competition, theoretically, should drive the clients of that shop to some other shop, and certain other shops would try to point out that the first shop was doing it if it knew, but there is a great deal of inertia among clients of one shop to change, and the chiseling retailer could certainly make this a bonus to his own profit.

From the point of view of society as a whole and injecting extra money, it does not much matter if it is a bonus to retailers—not very much—but such chiseling defeats the purposes of the bill a little bit, because it is to get the consumer to consume more, to increase consumption in relation to out put, whereas if the retailer gets the profit, it is like injecting money on the producer side of industry. The injection becomes wrong if the retailer chisels.

Very complex, but true; and there is more scope which is defeating partly the economics of the bill, and it is certainly a temptation to the retailer, and you may say, "Well, we can be expected to stop him." You can. You can have fines if he is caught, but I think there will be many lawsuits on that point, just as there will be many lawsuits on the definition of what is a retail sale.

I have nearly finished.

If this bill goes to the House, or probably it has already happened here in the committee, without the evidence being published, this point might arise. People will say to the authors of the bill that it is contradictory.

Mr. **Goldsborough**. May I say that the evidence will be printed before consideration of the bill is begun.

Mr. **Angas**. I beg your pardon.

They will say that the bill is contradictory in that, when it has been in existence for some time and succeeded in getting up the price level, as might be the desire to do, as should be, I think, the desire to do in this country, and then when the price level has gone to whatever you regard as ideal, say, 1926, to consider the ideals of another bill before the committee or about to be before the committee, then I am sure the author of the bill would like to put on the brakes and prevent a wild price inflation and the altering of the yardstick in dollars. In other words, he will want to stop prices rising any further, and those in charge of this measure, if adopted, the Federal committee——

Mr. GOLDSBOROUGH. The Federal Credit Commission.

Mr. ANGAS. The Federal Credit Commission, yes, will say, "We must stop prices rising. Maybe we have let them go a little bit too far. We must get prices down a little."

But look what happens as the result of the discount. This is not an objection to the bill; it is perfectly sound, but it is an attack which will be made on it, that the discount will be lowered from, say, 15 to 10 or maybe taken off altogether, if prices are swinging very fast, so that prices at retail will be raised to the ultimate consumer.

May I ask if you agree?

Mr. GOLDSBOROUGH. I do not agree, sir; but I am not testifying.

Mr. ANGAS. I beg your pardon; I just wanted to test my rationality.

A discount will be taken off by the retailer, and the ultimate price to the consumer will be raised. In other words the bill, when it wants to stop prices rising any further, the general price level as measured by index numbers—it positively raises the prices at retail by taking away the discount. It seems ridiculous and contradictory anomaly. Actually it is not at all. It is all right on that score.

Mr. FORD. It is a new limitation on purchasing power, is it not?

Mr. ANGAS. Yes; that is exactly it. That is just it, but everybody might not see this, and that is why I am mentioning it. If the Federal Credit Commission saw prices rising too far, and if they saw that consumptive demand was pressing at the moment too strongly on factory capacity, if they did nothing about it the price rise would go on up and up and up as a result either of factory capacity not being big enough, or, alternatively, as the result of monetary demand being too strong, and I think they ought to do something about it in order to preserve the purchasing power of the dollar and be fair to creditors, pensioners, and people who have quite rightly saved for their old age.

Mr. GOLDSBOROUGH. Anyone with a fixed income.

Mr. ANGAS. Yes. That is a part of my philosophy, that you must keep the dollar fairly stable in purchasing power. As I said in my evidence the first day I was here, Monday, the bill is right on this point, to raise retail prices, because that checks ultimate consumer demand in relation to factory capacity. That is very clever; very clever and ingenious, and on that theoretical score, quite faultless. You raise retail prices when you wish to check a general rise in prices, because of the influence of that on the prices charged by manufacturers and producers of materials, and because you raise the price ultimately to the consumer and he cannot buy so much, so that the pressure for the moment is taken off the producer to deliver, and prices do not get marked up by the producer, and that is a very able feature of this bill, in my view, immensely able, although at first sight it seems rather contradictory to raise retail prices when you want to stop a rise in the general price level, but it is a method of doing it.

Now, gentlemen, as I said at the beginning of my remarks yesterday, I do not intend to give evidence for the bill or against the bill. I will try to answer questions relating to the practicability of certain points, but, Mr. Chairman, I would ask you to excuse me from answering questions if I think to answer them would be an impertinence on my part.

Mr. **Patman**. I want to ask you——

Mr. **Ford**. Let me ask him this one question.

You said something about the fluctuating dollar. Let us take as an example a thousand feet of lumber. It is being sold at $10 a thousand today, and a week from now it is $15. What do we do? Do we change the price of the dollar, or change the foot measure, that is, cut it down from 12 inches to 9 inches? If we did, everybody would get up on their hind feet and yell murder, if we said that there should be 9 inches to the foot, or 8 ounces to the pound.

But we do that in effect when we say one day that $10 will buy a thousand feet of lumber, and the next day that $15 will have to be paid to buy it.

Isn't that a parallel?

Mr. **Angas**. Yes, it is a parallel; not a very valid one, though. It depends on your definition of the value of the dollar. It is getting back to the old, old question of the meaning of words. Some people say that money is sound if it is convertible into gold. I say money is sound not whether it is convertible or not. That is the Webster Dictionary point of inflation. I say money is sound if its general purchasing power is pretty stable. I do not want single prices to stop fluctuating in a single industry like lumber, or farm products, or anything else.

I think the law of supply and demand and the booms and slumps should be allowed to continue in a single industry as demand or supply changes. So what is true of the single industry, or what is reasonable for the single industry, does not seem to be reasonable for industry as a whole. Some commodity might be overconsumed or underconsumer, but I do not admit of the wisdom of a situation where there is generally overproduction or underconsumption. That is why I favor an index number to watch for the purchasing power of the dollar, as distinct from one in anything like lumber, in which there is bound to be a slump.

Mr. **Ford**. But you cannot overconsume anything. You cannot consume something that is not in existence.

Mr. **Angas**. It is the general problem that I am approaching, and I think the bill aims to approach it. You have today a lot of index numbers. I know a lot of index numbers. They are all hopeless, but the real bad index number is better than none.

Mr. **Patman**. I want to ask you a couple of questions on the bill.

If you were to make an effort to improve this bill, would you restrict these sales at a discount to those who actually need the discount, instead of giving it to all?

Mr. **Angas**. End of question?

Mr. **Patman**. Yes.

Mr. **Angas**. I do not think that that is an amendment which is applicable to this bill. An interesting feature of this bill is that it gives the discount to consumers with money, and not to the unemployed or the aged with no money. They have to have money to buy before they can get the discount.

Mr. **Patman**. You do not think that that is an objection, then?

Mr. ANGAS. That depends entirely on one's political philosophy. Some people say that money should not be given to those who have not earned it, or benefits given to people who are lazy and won't produce anything. Others say we should give money to the infirm and involuntary idle. What my views are on that political philosophy, I would rather not say, because perhaps, if anything I am a technical witness.

Mr. PATMAN. The other question——

Mr. ANGAS. I have a great sympathy for the man who is unemployed, but I would rather not answer on that point in this evidence, if you will excuse me.

This bill does not give the money direct to the unemployed. What it does is to stimulate total trade, so that there are fewer unemployed, but I would wish to be excused from commenting on whether it is best to give money directly to the poor and unemployed and the needy, or to create conditions where money will go them through general trade improvement, by implication.

Mr. PATMAN. There are a million and a half retailers in America. That includes all retailers, of all kinds.

Mr. FORD. As we define them.

Mr. PATMAN. As we defined them in the Government census.

As you stated, it seems almost impossible to define the word "retailer." But presuming that we can, and that we have a million and a half or two million retailers, and that we have 126,000,000 people. If this law is enacted, these 126,000,000 people, in making purchases for their own use, would be able to get a 15-percent discount. A corporation would not be privileged to receive that discount.

Knowing that some of the people, not all, but some, are always anxious to cheat, and we have evidence of that every day in the distribution of Government funds, I just wonder if it would be reasonable to put these retailers on their honor. If we did, then each one would have what would be equal to a check, all filled out, with Uncle Sam's name to it, and all that the retailer would have to do is to put in the amount, carry it to his local bank and get credit. He could say that he made a sale to John Doe of a $1,000 automobile, and he fills out this interbank currency receipt and carries it to his local bank for $150, and the local bank has to give him credit.

That gives to every retailer, the way I see it, to every person who is privileged under this bill to sell goods at retail, a check book with all of the checks signed by Uncle Sam that is good at any bank, and it is up to them only to decide how much they want to make the amount.

That is one side of it; that has to do with their honor.

Then, on the other side, if you attempt to check on these retail sales, there are billions of them. Everything from a package of pins to, I guess, a locomotive, can be purchased at retail. If we were to attempt to police, or investigate, all of these billions of retail sales, it would take more people than are now unemployed; it would take 10 million people to do it, and then I doubt that we would do a good job.

I want to say that I, too, am in accord with the objectives of the bill, but it just occurs to me that it would be absolutely impossible of administering, that it would open the floodgates to graft and corruption to the extent that everybody in America would be buying from some retailer and getting a 15-percent discount and selling it to another retailer, and letting him sell it and get another 15-percent discount, and it would put everybody in the retail business, and everybody would get rich in two weeks—and who would pay the bill?

Now, if I am wrong in my reasoning, I hope the gentleman will point out where I am wrong.

Mr. ANGAS. Peru.

If you are right in your statement or suggestion that it will require 10,000,000 people to police the 1,500,000 chiseling retailers——

Mr. PATMAN. There will be many more than that, because everybody will want a license.

Mr. ANGAS. I say, if you are right in that, there will be a boom in the legal trade of the country, and if you are right in your premises, I would not vote for the bill—and I hope I have not entangled myself in that answer.

About the amount of chiseling in the country, I am told that in Ruritania there is no chiseling.

Mr. PATMAN. If the legal profession were doing all of this business that you speak of, it would have to be paid in some form of money.

Mr. ANGAS. I thought that somebody would say that!

Mr. PATMAN. And that money would probably be worthless.

Mr. ANGAS. It may be.

Mr. PATMAN. The legal profession would not get much pleasure in working for nothing.

Mr. FORD. May I ask a question?

Mr. ANGAS. That was a dainty error.

Mr. FORD. I want to ask a question.

Do you believe, Mr. Patman, that the injection of a large amount of money would practically invalidate all money?

Mr. PATMAN. No; not an unreasonable amount; but here you would have no control. There would be not a dozen checks, but a million checks if they wanted to use them—and they would—and the Government would have already signed the checks and the banks would have to give them credit for it.

Mr. ANGAS. The bill provides——

Mr. PATMAN. You would have all the printing presses in America putting out interbank currency to keep up with the demand.

Mr. ANGAS. The bill provides for penalties; but then it might be a prison boom, and in the construction of prisons; and then, again—Peru!

Mr. PATMAN. If you were king, to use your expression, would you be willing to trust these fellows?

Mr. ANGAS. In Ruritania.

Mr. FORD. Who was the author of that?

Mr. GOLDSBOROUGH. Anthony Hope.

Mr. PATMAN. I shall refrain from asking further questions until I get more light on that point.

I am finished, so far as I am concerned.

Mr. GOLDSBOROUGH. Mr. Ford?

Mr. FORD. Yesterday I read to the Major a statement of our banking situation, and I would like to ask him a question on that.

Without boring the committee, I want to repeat the figures.

The total loans and investments in banks in the United States, that is, banks in the Federal System, amount to $31,750,000,000;

the total deposits, $40,350,000,000; the total reserves, $7,050,000,000; the required reserves, $5,850,000,000; and the excess reserves amount to $1,200,000,000.

According to the figures supplied to me by the Board of Governors of the Federal Reserve System, under Mr. Goldenweiser's signature, there are sufficient excess reserves at the present time to support a further increase in deposits of approximately $8,300,000,000. This volume of deposits of member banks is now as large as at any time prior to the depression.

With that situation existing in our banking system, the banks are certainly in a liquid condition, are they not?

Mr. ANGAS. Highly.

Mr. FORD. They are not only in a highly liquid condition, but they can at the present time loan six and a half times at least on $1,200,000,000, which would be about $8,000,000,000.

Now, if the businessmen of the country went into the banks and gave ample security and borrowed $8,500,000,000 more, and put that into production, what would be the effect on the present situation? Would that lift us out of the depression?

Mr. ANGAS. In my view, absolutely, if they would do it, but they refuse to borrow more, because they cannot sell what they have got, because the circuit flow of money is now frozen, as I described in that example yesterday. The businessmen won't borrow more to produce more, because the wholesaler won't buy his stuff, and the wholesaler won't buy it because the retailer won't, and the retailer won't because the consumer either has not any purchasing power or he won't use it through fear.

Mr. FORD. That is a preliminary question to another.

Mr. ANGAS. May I just add this, sir, that you might break this vicious circle of monetary stagnation by re-creating the expectation of a rising price level, so that retailers would change their policy and be willing to buy at present levels, and that would restore the expected flow of money.

The answer to your question is "yes."

Mr. FORD. If, in addition to that, we adopted a measure approximating the philosophy embodied in the Goldsborough bill, then what effect would that additional injection of interbank currency have on that particular banking situation? Would that tend to an inflationary period, or would it tend to maintain a balance between production and consumption?

Is that an intelligent question?

Mr. ANGAS. Yes, sir; I thoroughly understand it.

Mr. FORD. Leaving out the technique of how the thing would be done, assuming that it would be done.

Mr. ANGAS. Surely. There are first effects and secondary effects.

Mr. FORD. Like punching a pillow to make a hole in it on one side, and a bulge on the other?

Mr. ANGAS. The first effect of the application of this bill to the situation as it exists today would be to reduce inventories. The consumer discount would give to the public who have money today an ability to take in more goods from retail stores than would otherwise be the case. That would reduce inventories at retail. The retailers under the bill would get paid the full money as far as their own bank accounts are concerned. They would then probably replace their goods which they sold to the consumers by giving orders to manufacturers. They would probably not need to borrow any more from banks all of this eight billion surplus to which you referred as being in Mr. Goldenweiser's letter, so that on that score there would probably not be any more borrowing by the retailers from the banks out of that potential eight billion, unless the retailers decided to augment their inventories from today's level. Then they might borrow part of the $8,000,000,000 of the facilities now existing. I agree with the figures. They might or they might not, according to their inventory policy.

Now, let us look at the next step along the trail. We will cut out the wholesaler. He might increase or he might decrease his inventory. But let us go straight to the manufacturer. The manufacturer would, I think, if he did not happen to have a lot of idle funds, almost certainly borrow a bit from his banker, because his scale of production was increasing. It depends on the efficiency, but, taking the Nation as a whole, I would guess that there would be almost an enormous immediate demand on the part of the manufacturers for more bank credit which, when they spent it, would pass into the hands of the ultimate or semiultimate consumers.

So that you would get, in addition to the first inflation or expansion of bank deposits resulting from the consumer discount and interbank currency—in addition to that you would get, as a secondary result, some additional borrowing by manufacturers, so that there will be further expansion of bank-deposit money of a normal nature as a consequence of the operation of this bill, and insofar as that happened, bank-deposit money as a whole would be expanded, there would be more of it out and in circulation, and that would constitute an inflation of money in all of our deposits or, I should say, passbooks. I believe you say bankbooks more frequently in America. We say passbooks in England.

Thus you would get, as the result of that initial inflation of money, and of the operation of the bill, the secondary inflation of money, as happens normally in all periods of expanding trade. It would do no harm if productive capacity was so large that prices did not begin to rise. It would do no harm, as it were, to the purchasing power of the dollar. If the process went on continuously, you would probably find that consumption not only increased up toward factory capacity, but actually went beyond it in come cases, so that there was scarcity, as in numerous trades in December before last, December 1936, and after that it might tend to raise general prices.

As I have stated, I am in favor of a mild reflation of general prices in America today, seeing that the dollar has just risen 12 percent in purchasing power. I would like to see it back toward that 1926 level, so that it would fall maybe about 10 percent or so in purchasing power. After that point was reached, or if I personally had charge of the operation of such a system, before that was reached, when it became probable it was going to be reached, I would start drawing in the outstanding money in existence, bank money, by a mild credit contraction, so as to check in its early stages a dangerous upward price momentum before it had actually reached the dangerous level—or what I regarded as dangerous.

I would put on the brakes before I hit the stone wall, knowing that it takes time to slow down momentum in the economic system, just as it does when driving an automobile.

Mr. **Reilly**. Someone has said that one-third of our people are underfed, underhoused and underclothed. Would it be fair to assume that at least 50 percent of our people have plenty of money today to live on?

Mr. **Angas**. From a point of view of subsistence, undoubtedly yes. From a point of view of the Nation enjoying what the Nation is able to produce, I am not so sure.

Mr. **Reilly**. Assuming that to be true, what assurance have you from this bill that not to exceed one-half of the discounts granted under the bill would ever be paid out over the counters of trade of this country?

Mr. **Angas**. I rather hestitate to express an opinion on that, because it depends on mass psychology, but my own guess would be that if one adopted this bill under present conditions and granted the discount say next Monday morning, the 15 percent discount, it would have such an effect on the psychology of purchasing that probably by the following Monday mornning you would have to cancel the operation of the discount.

Put it in rather an extreme way, so as to indicte the tendency, just as today when there is as much bank credit in existence as Mr. Ford has said, quoting Mr. Goldenweiser, and I agree with the figures—just as there is so much bank credit in existence to drive the level of trade 30 percent greater than today, at a price level 12 percent greater, in other words as in 1929—there is so much monetary dynamite lying around in credit money deposits that anything that would cheer up the owners of that deposit money so that they would spend it again, thus restimulating the velocity of the stagnant pool of money—in other words, such a decrease in the store of value fear demand for money, if you could eliminate the fear, would, I think, send this price level up, whizzing up probably beyond the 1926 level before productive capacity had reached its maximum.

As I said yesterday, the mere threat of inflation, and a speech from high authority favoring the profit motive and the making of profits, might set in motion an inflation of prices today, resulting from a falling fear demand for money which you would have to check with the apparent contradiction that I, who advocate a mild inflation today, would be a few months later almost certainly advocating a deflation. I would be told that I was changing my mind. Just as a motor car driver steers to the left, correcting a swing to the right, and if he lets go to the left, he will get into the ditch. You have to swing it back.

And I think that in this bill, to get back to your question, sir, the adoption of it would set in motion such an anticipation of better trade and higher prices that it would be very necessary to take off the discount under present conditions.

In 1928, when there was virtually no fear money of this nature, no dynamite left around, this bill would not have lit up the dynamite because there was no dynamite.

Mr. **Ford**. May I interject? We have had a lot of talk about psychology and its effect on monetary policy. Isn't there a fear of inflation that might induce people to immediately run to the banks and take the money out, and try to put it away, or something?

Mr. **Angas**. No, sir, not in my view; at least not much, in my view, for this reason. There are various sorts of fear. If a quantitative monetary inflation is occurring or threatened, people become afraid of money itself, because its purchasing power is beginning to fall. So they try to buy into commodities, or something else, before the rise in prices. That is the fear of money, and it stimulates higher velocity, which tends to improve trade.

But fear of banks, or the people who create modern money, is a different thing. You can have fear of money itself without fear of banks as a place of safety. It might so happen that a fear of inflation, if it matured today in America, might give rise to a fear of a collapse in the bond market, and since the banks are institutions that invest or speculate more heavily in bonds, the public might begin to believe that the prospective slump in bonds would so weaken the cash value of the assets of the banks that some of the banks would on paper go bust, and they therefore might, seeing that happen, run to the banks, particularly those with a large quantity of long-term bonds, and withdraw their legal tender notes, thus causing a run on the banks, as you mentioned as a theoretical possibility.

Actually the threat of inflation in America today would not in my view have that effect, if it were a threat only. If there was actual inflation, there might be more of such an effect, but a bank fortunately is not only a speculator or investor in long-term bonds, but it has a lot of short terms which would not fall much, and it also has a lot of loan facilities on which it makes pretty good money, especially in a period of larger trade, and it also renders a lot of services, so although the banks may have a mild or even large depreciation on their bonds, they would be making more money profits in other lines of business and a lot of assets which they have received as the result of closing on mortgages, which would appreciate in value once more, so that I do not think that the public on the whole would run the banks on that score in this country as it exists today.

There is another reason why one need not, in America as she is today, fear very heavy collapse in the bond market, and that is because certain governmental agencies, like the Treasury, possess what is called the gold devaluation profit, which is now $1,800,000,000. It was originally $2,000,000,000. That can be used not only for buying gold and for an exchange, but also for supporting the bond market.

So I do not think the bond market would fall, because it would expect support, while the banks of the country have this rediscount facility, which tends to peg prices of bonds, so I do not think there would be any justifiable reason for making runs on the banks, or, in other words, any justifiable reason for fear of banks, even though confidence in money were slightly diminished.

Mr. FORD. Might there not be a swing to buy common stocks?

Mr. ANGAS. There would, sir, undoubtedly, and not for personal reasons, but for social reasons it would be desirable, I think, to see the stock market somewhat higher, not out of line with earnings, but I would like to see earnings higher, because the willingness of a nervous person to spend his income at normal speed depends on how rich he feels on paper. I do not want to see a stock market sky high, and foolishly out of line with earnings—of course not. It is socially dangerous. But, psychologically, since velocity influences trade, and since velocity is influenced by how rich one feels on paper, there is something to be said in considering the problem by itself in favor of stocks being reasonably priced rather than underpriced during periods of business depression. I do not say that they are underpriced today, but I think a rise in stocks tends to improve trade, just like improving trade tends to cause stocks to rise. They will react on each other. They can be too low, or too high—but I am rather diverging.

Mr. **Reilly**. Do you think the ordinary citizen is much influenced in his buying activity by talk of inflation or deflation?

Mr. **Angas**. It depends on the country, sir. In countries which have had inflation and deflation recently, like France, Germany, and so on, yes, very much; or even in countries like Holland and Switzerland, which have not had inflation, yes, sir.

Mr. **Reilly**. I do not refer to Germany or France, but I mean the ordinary inflationary talk that we have in this country.

Mr. **Angas**. Not so much as in other countries, but it would have an effect, definitely, yes.

Mr. **Reilly**. Do you not think that this bill would accomplish more in selling goods if a 100-percent discount were given to the man without money instead of a 25-percent discount to the fellow who has plenty of money?

Mr. **Angas**. I have not made the mathematical calculations, but speaking without having made those calculations carefully, and guessing, I do not think it would.

Mr. **Reilly**. Especially in view of the fact that a lot of these discounts may stay in the bank, if the fellow who gets it has plenty of money to live on. In other words, a man getting $5,000 a year is not going to increase his expenditures even if he does get a 15-percent discount on an automobile, in my judgment.

Mr. **Angas**. He might not increase his scale of expenditure, but he probably would a little bit, and he probably would save a little bit and invest it in industry, particularly if industry were showing great profits. There would, in fact, be a new revival. It might happen.

Mr. **Reilly**. Do you understand that the Treasury of the United States is back of and responsible for all of these discounts?

Mr. **Angas**. Do I understand that the Treasury of the United States is what?

Mr. **Reilly**. Who is responsible for this interbank currency? Who will have to redeem it eventually?

Mr. **Angas**. It need not necessarily ever be redeemed.

Mr. **Reilly**. But if it is to be redeemed, who is to redeem it?

Mr. **Goldsborough**. Can't you let him finish his answers, Mr. Reilly?

Mr. **Angas**. The Treasury ultimately; yes.

Mr. **Reilly**. Every year the Treasury would have to redeem probably 100 million dollars worth of it, would it not?

Mr. **Angas**. I do not think that it would have to redeem these notes for many years, but——

Mr. **Reilly** (interposing). The banks——

Mr. **Goldsborough**. Just let him answer.

Mr. **Reilly**. The banks are permitted to pay their taxes in this interbank currency.

Mr. **Angas**. Yes, sir.

Mr. **Reilly**. I understand that the banks pay somewhere around 100 million dollars a year in taxes to the Government so that much, at least, the Government would have to contribute every year, because it could not use that interbank currency for any purpose and it would lose 100 million dollars a year in taxes.

Mr. Angas. If the Treasury account or the budget account be separated entirely from the Federal Credit Commission account, the answer is yes.

Mr. Reilly. That the Government would lose that much money every year?

Mr. Angas. Yes.

Mr. Reilly. Would you mind telling me how the banks could afford to take this interbank currency?

Mr. Angas. I might add—I will answer that question.

I might add that if the bill was effective in producing greater prosperity, that the gross revenue of the Treasury from general trade improvement would almost certainly more than exceed the net deficiency resulting from the banks paying taxes in something that the Government could not pay out to the public again.

Mr. Reilly. In other words, if the bill works as contemplated, the Treasury could afford to pay 100 million dollars or so a year?

Mr. Angas. Yes, sir, as in England in connection with the early financing of the housing boom. It originally cost so much, but the net result was a surplus, although the pump-priming element of it was considered a loan and a deficiency.

Mr. Reilly. But how could the banks afford to take this interbank currency?

Mr. Angas. Because it costs them precisely nothing.

Mr. Reilly. But they have given real money for it.

Mr. Angas. No. sir.

Mr. Reilly. They have not?

Mr. Angas. No sir.

Mr. Reilly. Where did they get the money to give to the merchant who came in for the 15 percent discount on his sales?

Mr. Angas. They create it out of nothing by merely writing with a good pen an entry in the ledger to the credit of the retailer.

Mr. Reilly. I know merchants who have very small bank accounts. Their bank accounts are almost drained every month. They would have to make payments of real money to these merchants.

Mr. Angas. That, sir, is conceivable, but it is not in the bill. The retailers under this bill have to take money to the bank before they get the discount.

Mr. Reilly. That is under the provisions of the bill.

Mr. Angas. Yes, sir.

Mr. Reilly. But they could check it in on Saturday and take it out on Monday.

Mr. Angas. Yes, sir.

Mr. Reilly. Then wouldn't the bank be paying real money on those discounts?

Mr. Angas. Yes, sir; and that is why I raised the point, when Mr. Ford questioned me on that 2 days ago, and I said there may have to be some facility for converting part of these interbank currency notes into legal tender. The author of the bill who is sitting over there corrected me. I told him I was sure I was right. I am right.

Mr. Goldsborough. I still do not agree with you.

Mr. Angas. The point that the honorable member of the committee raises is that it is feasible that the creation of bank deposits by the member banks backed of course as to 100 percent by interbank currency can lead to the encashment of those newly created deposits, and the encashment of them into legal tender, so that the bank has to get the cash from out of its normal pile of cash reserves, and if the bank is already fully extended to the legal ratios, it would have to call in whatever the ratio was, 3 times or 10 times the amount of outstanding credit or investments to meet the cash drain resulting from these newly created deposits resulting from the bill.

Mr. GOLDSBOROUGH. Right at that point——

Mr. ANGAS. May I finish my sentence—unless you are interposing as chairman?

Mr. GOLDSBOROUGH. Oh, no.

Mr. ANGAS. I yield always to the Chair, naturally.

It is a point that can be raised. Theoretically it is a very important one. It might become very important in practice. That is why I hold my rather strong views on this, sir, in contradistinction to the author of the bill, and, like in many other instances I agree with him in some respects, though not in all respects.

Mr. GOLDSBOROUGH. What I was going to suggest is this: Of course, if it became necessary to convert any of this interbank currency into cash, it could be done immediately by the Congress, but what I called your attention to when we were discussing the matter informally was the fact that we have some 12 billion dollars worth of gold buried in Kentucky which can always be furnished to the banks by the Treasury or the Federal Reserve System if they need the cash, and that therefore that questoin is not an important one.

Mr. ANGAS. End of question?

Mr. GOLDSBOROUGH. Yes, sir.

Mr. ANGAS. I rather disagree with you, sir. It is the case of a single bank that I am talking about, and not the system as a whole. This is an important distinction on this very interesting point that the gentleman on your right has just raised. I agree entirely, considering the system as a whole, that if there was a shortage of cash in America today for the system as a whole, that your country has 12 billions of gold and certain silver facilities whereby it can increase the cash for the banking system as a whole without the slightest difficulty. It is already there when wanted. It is already available. But the gold might disappear some day——

Mr. GOLDSBOROUGH. Oh, well——

Mr. ANGAS. That is another point. But if this bill is to be a permanent measure, one cannot depend too permanently on the gold.

But as regards the single bank which the gentleman on your right was discussing, there is no reason why the Treasury should give that single bank a present, almost, of gold certificates, or whatever the certificates were, extra cash, legal tender, just because it alone was suffering from a demand for cash, because if the Treasury or the Federal Credit Commission gave legal tender notes to this particular bank that we are talking about, bank A, the directors of bank B would say, "Why give it to bank A? It is favoritism. Let us have some, too." Then everybody would be scrambling for extra notes from the Treasury on which to build further ratio investments or ratio loans.

So the point that Mr. Goldsborough raises about the cash being available is true of the system as a whole, but does not meet the case of a single bank, in my view.

Mr. REILLY. You recognize——

Mr. ANGAS. In other words, you are chasing a fox, which might be very important.

Mr. **Goldsborough.** You recognize this measure as an inflationary measure, do you not?

Mr. **Angas.** And deflationary. It is a method of managing money, injecting and retracting, and to tie the word "inflationary," onto it is wrong. It is not so inflationary as the gold mines in South Africa.

Mr. **Reilly.** Well, the author of the bill recognizes the fact that it is inflationary, for he has a provision for taking this interbank currency out of circulation.

Mr. **Angas.** To call it inflationary is just as rational as to say that General Motors is guilty of producing motorcars which will only turn to the right. It is neither inflationary nor deflationary. It has the ability to inflate or deflate, and one word without the other is not a fair description of the bill or of the Banking Act of 1935.

Mr. **Ford.** Would not "balancing" be a better word?

Mr. **Angas.** The title of the bill is not bad—no, the bill's title does not say enough about it, really.

Yes, it is balancing. It is on and off, hot and cold, up and down, brakes and gas, right and left, and, as I said, hot and cold, but not just hot or just cold.

Mr. **Reilly.** This bill provides, I believe, for a 15-percent discount after the bill has passed, until the Commission finds out what the discount should be. The counter turn-over of this country is supposed to be about 50 billion dollars a year.

Mr. **Angas.** Yes. I think it is much more.

Mr. **Reilly.** We will put it at that. Fifteen-percent would mean 7,500,000,000 of new interbank currency would be issued in 1 year.

Mr. **Angas.** Yes, sir.

Mr. **Reilly.** Would that effect the price of articles in the country?

Mr. **Angas.** If left permanently on, enormously. If the 15-percent discount was left on permanently, it would have an inflation similar to that of Germany, in my view.

Mr. **Reilly.** Would not that raise prices?

Mr. **Angas.** Of course. I just said so.

Mr. **Reilly.** Would not that decrease purchasing power?

Mr. **Angas.** Yes, sir, if left on.

Mr. **Reilly.** Then you would not get any result at all from your 15-percent increase in purchasing power?

Mr. **Angas.** If the bill were not operated wisely, and only the inflationary measures of it were applied and never taken off, the answer is yes, but the bill allows very carefully for the cessation of the discount whenever prices rise dangerously or when productive capacity lags—and that is a clever measure, because it does not need to wait until the price inflation has begun. It allows the discount committee to put on the brakes before that point is reached, just like one should, if one is running up against a wall, put on the brakes before one hits it.

Mr. **Ford.** If you let steam go into a cylinder one way, without any exhaust, you would not get any reaction beyond getting a bust of the cylinder.

Mr. **Angas.** Unless it was strong enough.

Mr. **Reilly.** If you had anything to do with the operation of this bill, you would inflate it how much?

Mr. **Angas.** Now?

Mr. **Reilly**. Do you think prices should go up?

Mr. **Angas**. I would not inflate at all. Did you say in the operation of this bill?

Mr. **Goldsborough**. He said, if you were in charge of the operation of this bill.

Mr. **Angas**. I wish you had said "of America."

This is not my bill, sir. I do not want to answer that question.

Mr. **Reilly**. Do you believe that the general price level is too low?

Mr. **Angas**. Yes.

Mr. **Reilly**. How much would you increase it?

Mr. **Angas**. I would aim at reflating the price level, measured by indices, about 10 percent.

Mr. **Reilly**. Wouldn't that cut down consumption 10 percent?

Mr. **Angas**. No, sir; because the price rise would come from an increase in consumption, a spending on commodities, and the expending and consumption would precede the rise in prices. Consumption would rise, and when it got strong in relation to inventories and in relation to new production, then and then only would you get your appreciable price rise.

Mr. **Reilly**. I refer particularly to that class of people who have not got too much to live on. If they only have so much, and you increase the price 10 percent, you decrease their ability to buy that much, do you not?

Mr. **Angas**. But the bill says——

Mr. **Reilly**. I am now outside of the provisions of the bill. You say one trouble today is that the prices are too low, and that everybody recognizes that the trouble is that people are not buying. If you raise prices 10 percent, the people who have a steady income are shut off from buying 10 percent of what they would usually buy, are they not?

Mr. **Angas**. Yes, sir; but I might plead for the protection of the Chair. You asked me the question, if I was in charge of the bill. The bill, to start with would lower prices at retail by 15 percent. Ultimately, I agree, it will set in motion a price rise, so that our original commodity, which would have been offered at $100 before the bill, will be priced in the shop at $85. That is the first phase of the bill. If the 15-percent discount is left on permanently, you will eventually get such a big inflation of deposits, and such a huge rush for commodities, that prices will rise, and the thing which was originally selling at $100 will probably now cost $150 if the bill is foolishly managed by the authorities and if the 15-percent discount is left on; that is, it will be selling at $150, less 15 percent, and so on.

The price rise will follow the price fall at retail, and if you leave the discount on the whole time, you will get the discount always below the figure that should have been charged, and all go up together.

This is the subtlety of the bill. The price fall at retail resulting from the introduction of the bill into practice will set in motion forces which, if not checked, and that is the important qualification, will send all prices up, so that eventually the point will be reached where the new price less the discount is higher than the original price; that is, if the bill is managed by people who do not carry out the details of the bill.

If I were forced to run the bill myself, I would put on the brakes when I thought I saw an unhealthy price inflation as distinct from a healthy inflation occurring. I would take off the discount when the price level was getting near the 1936 and 1926 levels.

I wanted to make that very clear, and I hope that you will not take offense at my giving you a very full answer.

Mr. REILLY. Have we not today plenty of facilities for raising prices if we see fit to use them? I refer to the Federal Reserve Board.

Mr. ANGAS. Will you say it more slowly?

Mr. REILLY. The Federal Reserve Board has all of the machinery necessary for raising prices, if it sees fit to do so.

Mr. ANGAS. The Federal Reserve Board, in practice, has not, without creating rather dangerous inflations of the bond market. Its only method of injection of new money is by the bond market, which is perhaps high. If you will substitute the words "the Government," or "the administration," and that is including the President and the Secretary of the Treasury—if you will include them, and use the words "the authorities," then my answer is "yes", that they have ample powers.

Mr. REILLY. I mean the Federal Reserve Board. The Board of Governors of the Federal Reserve Board have the power today to inflate, have they not?

Mr. ANGAS. A little bit; yes.

Mr. REILLY. They can inflate up to billions, as far as their judgment will dictate.

Mr. ANGAS. I agree that they can, but they have to get the money out through the bond market.

Mr. REILLY. The trouble is that they do not agree with you that prices should go up.

Mr. ANGAS. Let me answer that question on the technique of the Federal Reserve Board. They can only inject money through the bond market, which is a very narrow channel, and if they want to inject a lot of money quickly, they send the bond market just sky high, and when they stop the injection of money, the bond market probably cracks, after having been pushed up sky high.

The channel of injection of the bond market is much too small on occasions when fear is very great and there is a sudden increase in hoarding, like today, and I imagine that if you discussed this with the Federal Reserve Board, they would say: "Yes; we can inject, but we can not inject it fast without sending the bond market to dangerous levels."

I must not give evidence for the Federal Reserve Board, but I suggest that even those members who are most anxious to do something of a monetary nature to inflate or reflate find themselves stymied by being confined to the bond market. I am sure of that in my own mind, although I cannot prove it.

Mr. REILLY. Do you think that the Federal Reserve Board was justified several months ago in deflating when they increased the reserves of the banks, because they thought prices are too high?

Mr. ANGAS. I am aware that I am getting on dangerous ground, but I do think that they were justified in putting on the brakes early. I think the inflation of the years 1933 and 1936 was beginning to catch dangerously, and that if they had done nothing, you would have had an unhealthy rise in general prices in the course of 1937. I think they were wise to put on the brakes and raise reserve requirements.

Subsequently I may not have so much admiration for their actions. They stopped a depreciation of the purchasing power of the dollar which was showing its head around the corner, perhaps of a slightly unhealthy nature. Since then the combined results of their action and of 101 other things has led to a 12-percent rise in the purchasing power of the dollar. The yardstick has jumped about in a manner which is disastrous, in my view.

But the answer to your question is that I do agree that their action last winter was wise.

Mr. WILLIAMS. Right in that connection, do you believe that the Federal Reserve System under our present law has sufficient monetary control to maintain the price level when it is established at a certain point?

Mr. ANGAS. No; it has not. It can do a little on occasions where changes are very gradual, but when the crises occur, when big corrections are necessary, their powers are entirely inadequate.

I am confining my remarks to the Federal Reserve Board, working through the open-market committee. They have not enough power. The power is held up by other people, which is not, of course, the Board.

Mr. WILLIAMS. The reason I asked that is that there has been one school of thought that expresses itself in Congress pretty well along the idea that the Congress ought to give the Federal Reserve Board the direction to raise and maintain the price level to that of 1926.

Mr. ANGAS. And the question is——

Mr. WILLIAMS. Whether or not they have the right to do it, or whether they have the power to do it. In other words, would that be requiring them to do something which they cannot do under the present set-up?

Mr. ANGAS. Reading the 1933 Banking Act, and the 1935 Banking Act, and the President's inauguration speech on March 4, 1933, I thought the whole policy was to do that. The written evidence in favor of that being the policy is very strong. It was the declared policy of this country, and the implied policy, and I became more convinced that it was the implied policy when they put on the brakes last winter when the price level was dashing up in a manner which in my mind was unhealthy, even before the 1926 level had been reached, but you must put the brakes on early in this science or art, just like in driving a car; but since then it has been with complete amazement that I have observed the money managers doing nothing, not even using the powers that they have, doing virtually nothing to correct a 12-percent shrinkage of the average prices, a 35-percent shrinkage in Moody's wholesale sensitive commodity index, without even using the power which they have.

That has been one of the great perplexities in my mind in the last 6 months. It seemed to me that in September, when it became obvious to me that the fear complexes and other factors were about to initiate a trade slump, largely through fear and partly through previous credit contraction due to the banks selling bonds, that the Reserve Board would use the powers which it had, limited though they may be, but it has not. So I am in a state of wonder as to why not. I have my own personal views as to why they did not.

Mr. Williams. What do you say they should have done? What in your judgment should have been done, say, last September?

Mr. Goldsborough. Is that question embarrassing?

Mr. Angas. It is embarrassing, but the problem is so important socially that I think I will risk being quoted with headlines "Angas imagines himself as Governor of the Federal Reserve System and says what America ought to do," because that is about how I am treated in the press in the discussions of this important social question, and I resent it, because it is not fair.

I think it would have been beneficial last September if the Board of Governors of the Reserve System had used their open-market operation powers. I think it would have been more beneficial to the country that, instead of desterilizing $300,000,000 of gold on the 12th of September, and instead of saying that the reason for such action, which was probably the honest reason, was to meet in advance the possible Christmas demands of the banks for reserves or cash—if they had said not that, but something quite else, if they had said something like this, "We see around the corner the possibility, indeed the probability of the stock-exchange slump spreading to industry, and, if it spreads to industry, a serious decline in prices and a rise in the purchasing power of the dollar, and our function is, as we see it, to maintain the purchasing power of the dollar on an even keel, after having reflated it the appropriate amount after the 1932 slump and to keep it there as long as necessary, and anticipating a decline in the velocity of money resulting partly from the stock-exchange slump and partly from the factors which caused the stock-exchange slump, we propose immediately to do our best to meet that liquidity or fear demand for money by increasing the supply"—that is what might have been said, and I think it would have had a favorable influence on the sentiment of some people, the money bankers, the investors who are watching this problem more closely than, of course, the great masses of the people, but they control a lot of money, and therefore their state of mind can be easily influenced. Even though they are only a few in number, they are large in economic influence.

Mr. Ford. Major——

Mr. Angas. In order to give this answer, I must complete it, if I may.

And if the Board thought that their powers would not be sufficient, they might perhaps have taken the liberty of going to the other authorities who have much larger power and suggested that they cooperate not only with their quantitative actions but also with the aid of that most important monetary weapon, talk, which influences psychology, which influences velocity.

Mr. Williams. As I understand you, Major, they in your opinion have not the proper power to raise and lower prices and to maintain the price level as it should be maintained by monetary control?

Mr. Angas. No, sir; they have not. Congress still retains the real power. They have minor powers to influence comparatively unimportant movements.

Mr. Williams. What additional power would you suggest they be given?

Mr. Angas. It depends on the country and the banking system.

Mr. Williams. Well, of course, I mean our own banking system, and our country.

Mr. Angas. I would like notice on that question, sir.

It depends on the constitution of the Board and also, I admit, a little bit on the personality of the Board. As you know, the constitution now is that finance, agriculture, and industry should all be represented. There is also a qualification that there shall be geographical representation. The powers that you give to a board depend on its constitution, and, in my view, speaking as a person who wants the best solution, you must consider what human material you have available, what sort of man can be attracted to these high posts of control.

I doubt if any absolutely automatic system of money management will work. Several have been proposed. You might invent, possibly, an automatic system of guiding an airplane, or a ship at sea, but you cannot invent an automatic system of driving a car along the road with curves in it, and bumps, and where there is any psychology wind it needs men. You cannot eliminate the human factor in driving a car, and I do not think you can in guiding the money of a nation.

You asked me what powers they should have. It depends partly on the banking system, as I said. It depends much on the amount of trust you can place in the wisdom of a board, and maybe a little on the amount of trust you can place in their honesty. I am not so pessimistic as many people are about the honesty of the leading civil servants of the great countries.

The question should be considered very carefully by the representatives of the people. The question of wisdom does enter in it, and the question of the defined objectives that you give to a board.

Members of the present Board, in answering questions of reporters and in writing articles, have stated that they regard economic stability as more important than price stability. With that statement I agree over a period of years. But in recent months you have had so much price instability, due, in my view, partly to a change in the supply of money, but mainly due to a change in liquidity demand, that you have had neither form of stability. The objective of price relationships seems to have outweighed in interest the problem of the stability of the purchasing power of the dollar, and the eye seems to be focused in this country more on certain quite important side issues than on the main issue, and because of that and many other factors I think you have your slump and its continuance.

I cannot answer you what powers I would give to this Board without notice.

Mr. Spence. Could a stable, balanced price level be maintained by monetary management under any considerations? Are there not other nonmonetary factors that enter into it—for instance, competitive conditions, labor, and other things, and do not prices hold where the lines are strongest, and break at the point of least resistance?

Mr. Angas. Of course they do. The softest places give way first.

You won't get perfection from any bill. You will get amelioration, maybe. The index of prices—and I fully know the impossibility of the perfect index for anything; that is about all that you can look for—is such that no money manager will keep it in an exactly straight line, just as theoretically no driver can drive a car absolutely along the center of the road. He can keep it along the center of the road, but if one is meticulous, there is no such thing as the center of the road for the driver. There may be in one's imagination. Some prices will go up too high, and others will set back too much, and others will fall too low, but the capitalist system itself corrects that problem, if given time. If a price is unfairly high, or profits are unfairly too much, new capital enters the industry, if there is no monopoly, and when the new capital has had time to come to fruition, the increased supply leads to competition, and that leads to cutting the prices and the elimination of profits, and that is why booms in single industries are invariably followed by slumps. That is indeed the great merit of the capitalist system. The consumer ultimately gets the benefit resulting ultimately from the higher profit temporarily obtained in an industry.

Mr. LUCE. Major, the time approaches when we shall have to conclude this very profitable and helpful discussion, for which I thank you from my whole heart, but I would like to close my small share in the discussion with one general question; and, to absolve myself from any partisanship, I would say that in my judgment the Republican Party began a series of experiments with the Farm Board, and it went out of power and the Democratic Party continued the experiments, so that both parties share any responsibility or credit or blame.

We have seen now in the last 5 years a series of attempts to better the situation in this country by governmental activities, and to my mind they may be summed up in one phrase, the attempt to benefit the whole country by taking away wealth, or value, or purchasing power, as you choose to call it, from all of the people and transferring it to a part of the people. That is at the heart of all the farm legislation we have passed, and it is most notable in the matter of the bonus, the arguments being advanced that we could improve the situation if we could get out of the depression, if we take money from all of the people and give it to a number, in that case the veterans.

At the same time, in Alberta, an election was based upon the proposal of a method of taking value from all of the inhabitants and giving it to a part of the inhabitants.

Now, this long series of experiments which continue, for we are passing a farm bill every year to undo what was done in the preceding year—this long series of experiments will continue unless we reach the conclusion that the old principles were better, that you cannot amend the law of supply and demand, and that the competitive system has furnished the best way to conduct our affairs.

Do you, sir, as an observer of all of these experiments and of these proposals, because this is only one of a group of proposals with the same end—do you believe that on the whole it is wiser to continue these experiments, or to return to the law of supply and demand and the competitive system to work out their own problems?

Mr. ANGAS. I am delighted to have the opportunity of answering that question.

Many experiments were necessary in electricity, in aviation, in railways, and even with inoculation to produce improved results. So many experiments, I admit, are unsatisfactory. But good theory works in practice, and to dispute good theory is to be completely impractical in electricity, aviation, inoculation, and so forth, and also in the management of a currency. Many applied theories in the history of all countries have not been thought out, and that is why I express my admiration for this very patient committee, and thought is needed to cure what is obviously a ridiculous anomaly.

I am not going to criticize what I regard the faults of either this country or my country in the recent few years. I am more interested in remedies for what is wrong.

I am a believer in what is loosely called the law of supply and demand. Actually there is no one law of supply and demand. There are several laws, with which I won't bore you, which are completely contradictory, but I know what you mean and I know what is meant by the law of supply and demand, that careless expression that both of us use.

In the realm of money management which we are discussing in this bill, this bill itself to some extent, and my own writings to some extent, and the writings of many others to some extent, are aimed at making the law of supply and demand work in the realm of money which under the existing banking system which we have inherited from the past and which has grown up without having been originally planned does not work. In fact, the opposite works. As I have said on the first day of my evidence, at this moment, when the quantity of money should be inflated, or the supply increased to meet a growing store of value demand as proved by the falling price level, it is contracted, and that is what has happened in this recent slump. The store of value demand, as distinct from the medium of exchange demand for money, has increased very rapidly out of a fear, and simultaneously the supply has been contracted, so that, left to itself, without interference of the existing bank system, it disobeys automatically the law of supply and demand rather than giving rise to cumulative up-swings and down-swings which have been wrecking health as well as the economic prosperity since the modern banking system was developed.

I am therefore in favor of further experimentation in the realm of money, after further thought. Personally I think that thought has, I would say 10 years ago, gone far enough to apply any number of experiments which would be successful, just like when the Wright brothers got off the ground, and nothing else except sanely managed money will do it. It requires management, and maybe interference, but it will diminish the demand for interference and management in other realms of economic activity under any private behavior, and it will increase, in fact, the scope for personal liberty, in my view, and that is why I devote my life to what I believe in.

Mr. GOLDSBOROUGH. Major Angas, you came down here on Sunday and have been before this committee for 4 days for the purpose of trying to be of assistance to this country and to the world in helping to solve the problem of distribution, in trying to help solve the problem of poverty in the midst of plenty.

Speaking on behalf of the committee, I say with profound sincerity that we are all deeply grateful to you for coming and for giving us the talk that you have given us. We all realize that your contribution has been very, very great, and we hope to have the opportunity of having you with us again.

In the name of the committee, I want to again thank you very much indeed.

Mr. ANGAS. Thank you, Mr. Chairman and gentlemen.

Mr. GOLDSBOROUGH. We will meet tomorrow morning at half past 10.

(Thereupon, at 1 p. m., an adjournment was taken until Friday morning, February 25, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

FRIDAY, FEBUARY 25, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:50 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Farley, Mr. Meeks, Mr. Ford, Mr. Brown, Mr. Patman, Mr. Transue, and Mr. Luce.

The Chairman. The committee will be in order.

We have with us this morning Mr. Gorham Munson, of New York, lecturer on economics, who will discuss the bill we are considering, H. R. 7188.

We will be very glad to hear you, Mr. Munson, and you may proceed.

STATEMENT OF GORHAM MUNSON, EDITOR, NEW DEMOCRACY

Mr. Munson. Mr. Chairman and gentlemen of the committee, it would be rather relevant if I should state that I am the editor of New Democracy. That is a magazine which since 1933 has been advocating what is called the new economics.

This morning I thought I would talk chiefly on the administrative problem which has been discussed at these hearings, but before taking that up, I would like to speak on what seems to me to be the gulf between the old economics and——

The Chairman. Would you like to proceed for a time without interruption, or would you welcome interrogation at any time?

Mr. Patman. May I suggest, if the gentleman does not object, that he cover the second question first, the administrative provisions of the bill?

The Chairman. I think that is what he intends to do.

Mr. Munson. What I intended to do was to make an approach to that problem first, in order to see the problem in perspective, then I wish to treat that problem comprehensively and in detail.

The Chairman. You may proceed in your own way.

Mr. Munson. And the nature of that approach to the problem is such that I would like to have your permission to speak without interruption.

The Chairman. There will be no objection to that for a while, I am sure.

Mr. Munson. In the old economics it was said that if we let X equal the national production, measured in dollars, then X equals the national income. The old economics held that there was no inherent or chronic shortgage of purchasing power. So we have had various attempts to solve the economic problem from that standpoint. Those attempts have frequently taken the form of production credit schemes. There has been a succession of those from the days of Arthur Kitson, right after the war, to the latest scheme which we have heard here, the Cromwell scheme; or, still approaching our problem from the old economic point of view, we have had the solution of socialism. Socialism has said, "Let us socialize the ownership of production; let us redistribute income."

All of those schools of thought looked for the fault somewhere in production. They said, "We have to do something about production, and then things will straighten out."

When we come to the new economics, however, we find a different approach. We find the assertion that there is an automatic deficiency of purchasing power. We find that the reason for periodic breakdowns of our economic machine is assigned to a money system, which it is alleged is not in step with our increased productivity.

The economist, then, looks for the fault somewhere in the distributive system, and he tends to advocate aiding the consumer in some form, and he advocates consumption credits. This bill, it seems to me, would cure those faults through the national credit control account and the retail price discount. I would say that the gasoline which drives this economic invention, H. R. 7188, is provided by the national credit control account, that the engine is the retail price discount, and the feed pipe consists of interbank currency notes.

I have said this in order to give us some perspective on what I am coming to, namely, the administrative problem. It seems to me that the way in which one would approach such a bill as H. R. 7188 is this: Do we agree or disagree with the objective? On the whole, there has been very little disagreement with the objective.

Having decided that, we would next look into the method of the bill, and we would ask, Is this method technically sound? If we decide that the method is technically unsound, our interest in the bill, our discussion of it, stops at that point. What would be the use of going further?

But if we decide that the method is technically sound, then we come to the further question, Can the bill be administered? Is there an administrative problem connected with this bill?

It has been my privilege to attend many of these hearings, and so far as I have heard, there seems to be general agreement on the objective of the bill, but there has been, I should say, comparatively little technical discussion of the discount principle in the bill—I say comparatively little, because there has been some intelligent and acute discussion of that, but it has happened that there has been much discussion on the part of certain witnesses, as well as on the part of the committee, of the administrative problem. I have the feeling that that discussion has been somewhat disproportionate.

The idea of a scientific price calculus, based on a ratio of consumption to production, has been discussed considerably in this country since Mr. Goldsborough's first bill, H. R. 9216. I am familiar with that discussion and with the attacks made upon it, but very seldom in that discussion has the ground of attack been along administrative lines. I think that is because that attack is based on a weak position, to begin with. What I shall try to demonstrate in the next 20 minutes or so is that the administrative objections raised to this bill thus far on examination have been found to be exactly 1 inch high, and yet they have been put forward as insuperable or extremely difficult objections.

Now, it is obvious that this whole matter of how to administer this bill is a question for experts in administration. It is something which should be put up to men who are trained in their daily work to deal with such problems.

It so happens that the scientific price calculus has had the support of a number of men who are accountants, who are administrative experts, who are directors of large companies, and the like, who, in considering their support of such a principle, have looked at the administrative side and said that it is perfectly feasible from the administrative point of view.

Two or three years ago, when Mr. Goldsborough's bill, H. R. 9216, was being studied, Mr. J. Crate Larkin, the vice president and treasurer of the Larkin Co., in Buffalo, became interested in the whole idea, and, having convinced himself that the principle was technically sound, he said: "Now, let us go into the administrative side. I am going to turn this whole idea over to our accounting department in the Larkin Co."

That company happens to do a manufacturing business, a wholesale business, a fairly large mail-order business, and a retail business. It had two or three chains of stores through the Middle West. It is a fairly good-sized company. I have described it because you can see that such a company brings in all of the administrative problems so far as industry is concerned.

So Mr. Larkin turned over the proposition to his accountants and said: "Go to work on this. Report back to me and tell me if you find any difficulty in our company in operating under such a system as is proposed by Mr. Goldsborough's bill"—and I am referring to his former bill.

Well, as a result of considerable study by their department of accountants, the report came back, and it was: "We could work this with ease. There would be no administrative difficulties on our side in case such a retail price discount was declared."

Now, I submit that the administrative difficulties which will come up under this bill should be referred to people engaged in administration. They should be asked: "Do you find any insurperable administrative difficulty in operating your business under a retail price discount system?"

At this point I would like to submit for the record a letter of mine which was referred to a week ago today. One of the members of the committee referred to this letter and somewhat erroneously reported its contents, due, I am sure, to the lapse of time of 8 or 9 months. But since the letter as referred to by the member differed from what the contents actually are, I would like, if I may, Mr. Chairman, simply to have it incorporated in the record.

Mr. Patman. I would like to know what the letter is.

The Chairman. I was going to ask that myself. I did not hear the gentleman's statement, for I was called out. I am sorry.

Mr. Munson. The letter is a letter to Mr. Patman, and you will recall that——

Mr. Patman. Who wrote the letter?

Mr. MUNSON. It is a letter from me.

The CHAIRMAN. That is a part of your discussion?

Mr. PATMAN. You sent me the letter, did you?

Mr. MUNSON. Yes, sir.

Mr. PATMAN. And that is where you said that the chicken peddlers could get licenses?

Mr. MUNSON. You may recall that in questioning Professor Weyforth you referred to receiving a letter from a former witness, and you made at that time a summary statement of what that letter said. Now, as I have just explained, the letter having been sent to you some 10 months ago, it is only natural that your statement, relying upon memory, should not in my opinion represent what the letter actually did say, and for that reason I would like very much to have this letter incorporated in the record.

The CHAIRMAN. That will be done, without objection.

Mr. PATMAN. I do not object.

It is the letter where you said that an egg man could get a license to sell—

Mr. MUNSON. That is correct, and also——

Mr. PATMAN. In other words, if he got a license to sell eggs, he could sell automobiles?

Mr. MUNSON. In the case of the letter, that question did not come up.

Mr. PATMAN. I have no objection to it going in.

(The letter referred to is as follows:)

NEW DEMOCRACY, INC.,
New York, N. Y., July 29, 1937.

Hon. WRIGHT PATMAN,
House of Representatives, Washington, D. C.

MY DEAR MR. PATMAN: I greatly regret that we were both so restricted by considerations of time at the hearings on H. R. 7188 yesterday, and I regret further that I was unable to remain over in Washington and reappear for questioning by you today. The art of giving brief answers that really clarify is dependent upon the well-formulated question which narrows the field to an area in which a precise brief answer is possible. I gathered from the colloquy of the chairman, yourself, and myself that at least one of your questions—that having to do with the licenses of retailers—while seeming to be within the context of the bill actually arose from a context outside the bill, namely, State licensing of retailers. I will therefore review our questions and answers so that you may clearly understand my views.

You asked if H. R. 7188 were a Douglas bill. I replied that it was derived from the Douglas ideas. The full meaning of this statement is: The Douglas principles have been abroad in the world for 20 years and have inspired a world movement. They are, like all ideas made public, anyone's property. H. R. 7188 originated entirely outside any formal movement for social credit and departs from Douglas in certain respects and incorporates other ideas in certain provisions. It is an independent piece of work which, when examined by technicians in the Social Credit movement, has been found sound.

You asked if I were the spokesman for the Douglas movement, and I replied that there was no official movement in America. I am an advocate of Douglas Social Credit but claim no title to speak for anyone but myself. Douglas has no official representative in this country, and in England only the Social Credit secretariat of which he is chairman can speak for him. This is a matter on which especially I wish you to be clear.

On the question of retailers' contracts with the United States Treasury: It must first be grasped clearly that such registration to dispense the discount is entirely voluntary and a matter to be decided according to the business judgment of the firm. In the case of your hypothetical farmer selling eggs, etc., to the neighborhood, I would have asked you in turn if our time had permitted, how much retail business you imagined him as doing. If much, he would probably wish to register for the discount, which would be advantageous to him. If little, say some sporadic selling to a few summer residents, very likely he wouldn't bother. Small businesses on low-priced retail articles probably wouldn't come into the scheme unless the discount were considerable. Even big businesses, like 5-and-10-cent chain stores, might stay out. The public would not be much concerned with a saving of a penny or two on a small article. Thus, your hypothetical small farmer if engaged in a little retailing on the side might conceivably do perfectly all right without any discount apparatus; he would be peddling, let us say, fresh milk and eggs direct from farm to consumer; and the consumer might in this case gladly pay a little more than the stores charged.

In respect to lower prices: The correct answer was the one I gave you, namely, the Social Credit aim is the increase of purchasing power. Lower prices to the consumer is the mechanism for increasing purchasing power (it is anti-inflationary, as you of course understand). It's lower prices in front of the retail counter. In back of the counter however it's the full financial price that is received. It won't do to mix up the psychology of the consumer with that of the producer. The producer gets his full price via cash received from consumer plus discount voucher mark-up at the bank. In brief, the scheme is lower prices for the consumer, full price recovery for the producer. You appeared to feel that there would be enforced a lowering of prices among the wholesalers and prime producers. It would not be enforced exactly, but for perfectly natural reasons we can anticipate lower costs in the chain of production leading up to the shop counters. I will take a separate paragraph to explain.

I mean something more than lowered unit cost as the volume of production rose to meet the increased demand that would be brought about by H. R. 7188. I mean there would be increasing total profits all the way back to the prime producers. How would they be used? The practice of building up large reserves would undoubtedly be discontinued. Shareholders would put pressure on directorates to distribute profits as dividends. More than that, there would be a tendency to use part of the profits to pay off short-term bank advances so that the day-to-day working capital of industry would become the absolute property of business firms. This would be money in rapid transfer between various producers. It would not create new costs but merely transfer existing costs. This means the progressive emancipation of business from banking—something I believe you favor in your own proposals for the restoration of small business—and it means lower producers' prices because allocations to reserve, etc., are no longer necessary. The legitimate allocation for depreciation would of course continue.

I am sorry that your question about the national dividend was never completely formulated.

This morning the new issue of Dynamic America reached me, and I see that we have articles side by side. I found the information in your article, Concentration of Control in Industry, very well presented and it will be very useful. Social Creditors aim to decentralize finance, to do away with the very centralization of money which you so effectively point out. And there is no question in my mind that the institution of Social Credit would mean the revival of small enterprises, an aim of yours I am in hearty sympathy with. With your financial proposals, however, we must disagree. They would strengthen the existing principal defect in our financial system rather than correct it.

Faithfully yours,

GORHAM MUNSON.

Mr. MUNSON. Now, we come back to this question of fraud, the question of administering the bill. We have first of all to consider the incentive to fraud. The incentive to fraud under the present system whereby the population is short of money appears to be very high. Sociologists making a study of crimes have generally agreed in saying that 90 percent of the crimes committed today have a financial motive, and that, I submit, is a very strong indictment of something or other in our society, that 90 percent of the crimes today can be traced back to a financial motive, so that we know that a good deal of crime today has its origin in money stringency.

Now, I ask, would there be, under the operations of the bill designed to loosen the squeeze, designed to improve the condition of the people, designed to make money less scarce—would there be under the operations of such a bill as much incentive to crime as there is at the present time?

Then, in thinking of fraud in connection with such a bill as H. R. 7188, we have to reckon with first of all a decreased pressure on the citizen to commit fraud. We have to place that citizen in a society in which there is more purchasing power and say, "Would you, under those conditions, be as much tempted to commit crime as you are at present?"

This is not to say that a fraudulent tendency would not persist in human beings. Nobody is saying that. There would, of course, be this tendency in human nature; we would expect under this bill or any other bill a certain amount of cheating, but I want to make the point that the pressures put upon people to cheat would be relieved by this bill.

The next thing that I would like to say about this bill in connection with the question of fraud is this, that this bill operates along the lines of human desires. It does not go against them. On the one hand you have your producers, you have business, and it is clamoring for orders; it wants to sell; it wants buyers; it wants a strong market. This bill proposes to aid business in that natural desire.

On the other hand, you have the consumer who wants to buy, who wants to raise his standard of living, and the bill comes to his aid. You see, this is very different from an unpleasant law, like, let us say, the prohibition law, which seemed to be in conflict with many human desires, and, being in conflict with them, stimulated people to evasion. Here you have a bill which runs along the desire of business to take orders.

So, what we propose to show is this, that under this bill fraud would be difficult, it would be unprofitable, and it would necessarily be on a small scale. Let us take up, first of all, the case which has been mentioned here, of fraud between consumer and retailer. We have been told that an article might be sold, taken back to the retailer, sold over again, and that the same article might be sold many times. The point about that, however, is that very soon, when that was practiced on any scale, the books of the retailer would show simply this, that many more articles were being sold than the retailer was buying.

So far as producers are concerned, they cannot get in on the retail price discount, but it has been pointed out that a corporation might arrange with a private citizen to buy for it.

Mr. PATMAN. What will keep a producer from getting in on it? Can't he get a retailer's license?

Mr. MUNSON. Then he becomes a retailer.

Mr. PATMAN. And also a producer.

Mr. MUNSON. That is correct. In the case of the Larkin Co., you have a manufacturer and you have a retailer.

Mr. PATMAN. A fellow would be foolish, with this bill in operation, not to also get a retailer's license if he were a producer, would he not?

Mr. MUNSON. Not necessarily. I doubt if many prime manufacturers, many firms dealing in the producing end, would want to get into the retail business.

Now we come to the corporation which it is thought might engage a private person to buy for it in order to get the benefit of the discount. The proposition is something like this, that a citizen goes out and says, "I am an ultimate consumer, and I want to buy such and such a thing." Then there ensues a special kind of second-hand sale. He has purchased an article which a corporation wants, and he goes to the corporation and says, "Now we have made a deal; I have the discount on this. I will turn it over to you on some kind of a 50-50 split, let us say." So we have here a picture of a special kind of a second-hand sale.

Now, let us go into that just a little bit. To begin with, a great many corporations engage in quantity buying. The corporation that I worked for until a few months ago, when the latest stumbling of the economic machine knocked it over, did a certain amount of quantity buying; that is, it bought paper by the carloads; it bought printing, and the printing of 75,000 magazines, and this sort of quantity buying is obviously out so far as any classification of retail trade is concerned; it is obviously out of the picture for an individual to go and say "I want to buy a carload of paper for my personal and family consumption.

So then, sticking to this little corporation with which I was connected, let us see what it could do along the lines suggested. Well, it needed office furniture. They spent, I believe, about $300 in office furniture. If we had gone to some friend and said, "Here, you buy this office furniture at the retail price discount"—that would be $45 off—"then we will make a deal with you for its resale to us," and we would have a citizen doing the following awkward piece of work: He would have delivered to his home four or five desks, office chairs, hat racks, and so forth. He would then have to have that carted to the office, at an expense of $10 or $15 on a $45 discount. Then let us say that there is a split of the balance. The corporation saves $15 on the purchase of its office furniture and the individual gets $15 as a result of this circuitous deal. That is easily detectable.

Then let us take a more minute example, still sticking to the same corporation, which would be a more logical example——

Mr. PATMAN. Who will detect that?

Mr. MUNSON. I am coming to that in a moment. I am going to speak of the penalty provisions of the bill, and of the administrative set-up for detection. Just at the moment I want to follow rather closely the workings of this particular deal.

Mr. PATMAN. Will you state who is supervising it, who is watching it?

Mr. MUNSON. In the case of this corporation, it might have been reasonable to say that it needs a typewriter, and it will get somebody to buy the typewriter at retail. Let us say that we need a $50 typewriter, and there would be $7.50 off as a retail price discount. The typewriter is brought in, and there is split $3.75 apiece. Well, the corporation has saved $3.75, and the pseudo-retail buyer has gained $3.75. The corporation has lowered its cost by that same sum. It might conceivably pass this lowered cost on to the consumer, and it might be spent; it might be put in reserve.

But now let us see exactly what has happened by this small piece of cheating. The man who has bought the typewriter has signed a voucher, and the voucher has stated that in making this retail purchase he is securing the article not for resale, for trade, or manufacture.

Mr. PATMAN. But Mr. Goldsborough has said that the purchaser would not have to sign anything. He is the author of the bill.

Mr. MUNSON. The bill necessarily does not cover all of the details of administration.

Mr. GOLDSBOROUGH. My view certainly was that the purchaser should not be in the picture at all in that illustration that you are referring to.

Mr. MUNSON. In the case of the retail sale, in the case of this typewriter, you go into the typewriter shop, and, as the ultimate purchaser, you put down your cash and you have your discount. Now, the bill naturally does not cover the printed form of the voucher which might be signed by the buyer of that typewriter, but I assume that in order to get this consumption credit, a printed slip is handed to the buyer, and he signs, signifying that the sale has taken place. The printed slip could very well cover the provisions of this bill, that a purchaser at retail is one who is purchasing for his personal or family use and not for resale, trade, or manufacture.

I further assume that in the administration of this bill, the retailer would then take the cash and the signed vouchers to the bank, in order to be credited for the vouchers.

Mr. GOLDSBOROUGH. It could be done in that way, but I think it would be impracticable, and in my statement I have left the ultimate consumer out of the picture.

Mr. PATMAN. But suppose that he bought that for personal use, in good faith, and the next day he sold it, and then you attempted to prove that he did not buy it for personal use, and he said "I did, but I changed my mind." How will you prove that he did not change his mind?

Mr. MUNSON. We are coming ultimately to the picture of second-hand sales, but I will say this, that there are alternative ways of administering the retail price discount. The bill does not have to prescribe the precise way to administer it.

For the purposes of visualizing how it will work, I have always thought of the sale being made with cash and the customer simply signing a formal slip, which happens to be a practical way of doing it. There are other ways by which that could be done.

Very well. We have in my picture of the operations of this bill, then, a man who has bought a typewriter at retail, passed it on to a corporation, signed a voucher stating that the purchase was not for resale, trade, or manufacture, and he has run the risk of coming under one or another of the penalty provisions in this bill for the sake of a $3.50 take. The corporation likewise has run the risk of coming under one or another of the penalty clauses of this bill for the sake of that small saving.

Now I come really to the central point, and that is that this petty piece of cheating does not affect the economic system. Your typewriter has come up to that counter with a price on it, a thing which is industrially used——

Mr. PATMAN. You can use the illustration of the automobile as well as that of the typewriter, and it would be a better illustration.

Mr. MUNSON. I am coming to the automobile illustration, but for the moment I want to follow very closely this particular point, because it ultimately runs into the complete picture of absolute lack of harm to the economic system. I say, even if practice, the damage done to the economic system would necessarily be on a small scale.

Now, the manufacturer, the wholesaler, and the people who brought that typewriter into that shop are interested in one thing, in liquidating the costs embodied in that typewriter.

Your retail buyer has come in and put down his cash. The voucher has been made out and deposited at the bank, and the retailer is in position to send the money back to the wholesaler, the wholesaler to the manufacturer, liquidating those costs. The costs of that typewriter, from the economic point of view, have been met by the cash of the consumer, plus the retail price discount voucher, and that is why I said that it goes into the category of a special kind of second-hand sale. I ask you to consider, as a side problem, the problem of second-hand sales.

Mr. PATMAN. Before you get to second-hand sales, suppose that a merchant carries cash in the amount of $850 and a voucher for $150 from the customer to the bank. Evidently this voucher would have to be specific. It would have to give dates. It would have to give a description of the article shown. There would be considerable book work in connection with that, but we will presume that he has done that and he wants to get credit at the bank. Would the banker have a right to refuse that, or would it be left entirely to the retailer?

Mr. MUNSON. If the sale is a valid sale, the banker has no right to refuse it.

Mr. PATMAN. All right. Now, then, suppose that this is a forgery. Suppose that the dealer says "Well, John Doe came by my store a couple of days ago, and I sold him this car for $1,000, and I want this $150," and some agent of the Government came to him and asked him, "Well, who is John Doe?" He would say, "Well, I do not know." The Government agent would say, "Where is he from? Is he from Georgia, South Carolina, Texas, or New York?"

"Well, I do not know. Here is his receipt."

Wouldn't you have any right to question him on that?

Mr. FORD. The sale of an automobile is not that simple. There is State registration, and a whole lot of other things. Don't use an automobile for that illustration.

Mr. PATMAN. We will take a span of horses, if you want, or a race horse, or anything else. How would you detect frauds like that? The burden of proof would be on the Government to disprove it, and the man has gone. You could take any purchaser and say that he came in and bought four or five suits of clothes, and several pairs of shoes, and it would be a very difficult matter for the Government to prove that the retailer did not sell those to that party. You would have to take the 126,000,000 people of the United States and line them up, and find that buyer.

Mr. MUNSON. At the present time we have got this for, however; we are dealing with the incentive to fraud, and I am specifically trying to show that it would operate on a petty scale, and it would be a great nuisance to offer to go to work to perpetrate fraud.

Now I am asked what about the system of inspection. That, I submit, would come further along the line. We must first understand the actual working of fraud, and then the next problem would be the degree of inspecting needed.

Mr. PATMAN. Before you get off the fraud, let me ask you this question: Let us take as our example a store like that of the Hecht Co., here in Washington, a large department store. They have several hundred clerks. Each clerk, I presume, would finish the transaction that he was handling, and then all of these hundreds of clerks will bring in these vouchers at the end of the day. You would not carry these hundreds of clerks down to the bank to get the interbank currency. The manager of that store, who did not see the purchasers at all, who does not even know, in fact, that the sales were made, would go to the bank and say, "Here are the vouchers; give us the credit."

Wouldn't that be issuing money on hearsay?

Mr. MUNSON. Well, a great deal of the business today runs on what you call hearsay.

Mr. PATMAN. We have not started issuing money yet on hearsay, have we?

Mr. MUNSON. I am not so sure.

The second-hand sales are very relevant to the problem that we have been discussing. If you think of second-hand sales economically, you think of a block of effective demand which, so to speak, is quite apart from industrial costs and the liquidation of them. Costs, so far as industry is concerned, are liquidated only the first time that a machine is sold. Then it goes into the second-hand market, and that is merely a transfer of payments from one person to another, but it does not do anything further to liquidate costs in the industrial mechanism.

Very well; now, in the case of this example of fraud, the primary purpose of selling the article on the part of the industry to somebody has been accomplished, and that sale does something about liquidating industrial costs. Whatever happens after that is necessarily a second-hand selling, this block of effective demand circling from person to person but not going back into industry to meet any costs involved in that article. There is a second-hand sale problem, but this bill does not tackle it, and it is not important that is should. Ultimately it would have to be tackled, namely, you should have in a financial society the money in existence not only to meet production costs as they come up to a counter, but also sufficient money to meet second-hand transactions, but it is very important, it seems to me, to consider that this petty example of cheating does not affect the cost structure of industry, that it is in the second-hand field.

Now, another thing to consider in respect to corporations buying along the lines proposed is wholesale and jobbers' prices, which are discount prices already. In the book field, for example, your book store gets a 33⅓ percent discount from the retail price in buying books, so that nobody could go around buying books at a 15 percent discount and sell them to a book store. He would have to get, at most, the second-hand book price, which is usually——

Mr. FORD. Two bits.

Mr. MUNSON (continuing). Twenty-five percent of the list price. So that when you figure on a corporation saving money by manipulating a private individual to make purchases on a 15 percent discount, you have to figure on a comparison of that with jobbers' or wholesalers' discounts.

Mr. PATMAN. But suppose he buys this automobile. I will go back to an automobile. He will fill out that slip, with the number of the car, the description and everything, and he buys that car in good faith, and the next day he goes to the bank and gets the $150 discount on a $1,000 car, and after that, in good faith absolutely, he sells it to a second-hand dealer for $925, and this second-hand dealer turns around and sells it for $1,000 as a brand new car and gets $150 from the Government again. I say, that is done there in good faith; there is no fraud about it.

Mr. MUNSON. It is quite possible, but second-hand dealers are not in the habit of paying quite as high a price as that.

Mr. PATMAN. But it is not a second-hand car. It has not been moved off of the floor. It might be sold a dozen times, possibly, before it is moved off of the floor.

Mr. TRANSUE. Isn't there a considerable practice in that field on the part of dealers who are loaded with automobiles to give part of their discount to second-hand dealers?

Mr. MUNSON. It may be.

Mr. TRANSUE. The automobile companies have to fight that particular thing all the time, to be sure that their dealers are not selling to second-hand dealers at a list price and then giving part of their discount away.

Mr. MUNSON. Mr. Transue has brought in another element, namely, the vigilance of the trade associations regarding the ethics of their individual members.

But now this is a point being made about a sale to a corporation. The corporation has gone, we will say, to all of this trouble for a profit on a petty sale——

Mr. TRANSUE. We are not talking about corporations, but about individuals.

Mr. MUNSON. I have not quite finished with the corporation. What I was endeavoring to point out is this, that the corporation has this problem of full cost recovery that is going to be made by the retail sales of articles made by this corporation, and the retail price discount comes in to enable full cost recovery.

Now, the corporation facing that picture, we are then asked to believe, would say, "We are going to botch this picture in some way; we are going to try small tricks, to enable us to get our costs back," and when this is discussed, we have to keep in mind the five or six paragraphs of penalties, on the risks involved, and is the corporation going to go out of its way in the manner suggested for a small take?

Mr. PATMAN. Right there, suppose that the Willard Hotel has 300 rooms. I do not know how many they have, but we will assume for the purpose of this illustration that it has 300 rooms, and that they rent those rooms at $10 a day. That is $3,000. Each morning, under this bill, the manager could go down to the bank and collect $450 from the Government. That would be 15 percent of $3,000.

Now, if Mr. Goldsborough is right, that there would be no supervision at all——

Mr. GOLDSBOROUGH. I did not say that.

Mr. PATMAN. I understood you to say that there would be no signing up of any kind by the consumer.

Mr. GOLDSBOROUGH. What I said was that in my conception of the administration, the consumer himself would not have any part in the transaction.

Mr. PATMAN. That is right. That is the way I understand it.

Mr. GOLDSBOROUGH. I did not say there would be no supervision.

Mr. PATMAN. Therefore it would be left up to the manager to state that all of these rooms were rented at $10 a day, in order to collect $150 each day from the Government.

On the other hand, if you are right, that you would have supervision, and it would have to be close supervision, you would have to have a lot of Government people around the Willard watching the thing, and it would take a large number of people in each store; there would have to be one to each clerk, because that would be the only way that you could properly check on it, and there are at least 4 million people in America—I believe that is a safe, conservative guess—engaged in business that would come under this bill, and I mean clerks and all who would be making sales to the public.

So it would take a lot of people to supervise all of these millions and billions of transactions, and if Mr. Goldsborough is right, that the consumer would have no part in it, it would just open the flood gates of fraud and corruption, and would just be putting every retailer and every clerk on his honor. I think that that would be bad.

On the other hand, if you are right that you would have close supervision, it would take at least 4 million people, or maybe 6 million people, to properly and adequately supervise it.

Mr. MUNSON. Of course, you realize——

Mr. REILLY. That would cut down the unemployment.

Mr. MUNSON. You realize that you have made a reductio ad absurdum of your own argument, because the question was that——

Mr. PATMAN. If it is absurd, the bill is absurd, because it is based on what the bill requires.

Mr. MUNSON. The question is, on this line of reasoning, How is it any law is ever enforced?

Mr. PATMAN. It takes lots of people to enforce it. Take prohibition. Look at the number of people they used, and they could not enforce it.

Mr. BROWN. Suppose that we have a chain store and an independent merchant, and they both sell flour. Suppose that the independent merchant sells a small sack of flour at $2 a sack, and the chain-store merchant sells it for $1.70 a sack. Would the independent merchant get his discount?

Mr. MUNSON. Yes; the buyers from both merchants, if they voluntarily took out contracts to dispense the discount, would receive it. You would have the same rate of discount, 15 percent, on both purchases. You see, Fifth Avenue prices and Sixth Avenue prices would remain relatively the same as they are now. The discount would be the same if you moved from Fifth Avenue to Sixth Avenue. It is the full discount everywhere.

Mr. BROWN. It seems to me that, in order to be equitable, there ought to be a standard price for the same article in the same community.

Mr. MUNSON. I think that is getting into the field of impracticability, but I do think—and this is an aside—I do think this bill would lead to the revival of small business, would enormously strengthen small business, but that is another point.

Well, to get on with what I said at the outset was an attempt at a comprehensive discussion of this fraud, the question has lately been raised that it is impossible to define retail trade with a razor-sharp edge, which I think we would all grant. Nevertheless, retail trade can be fairly well defined and it is fairly well defined and is practically defined in this bill.

But we come to certain border-line cases, and this is an administrative problem somewhat more difficult than any that has been presented thus far. What would your border-line case be? You have a physician. He wants an automobile. The automobile is partly used by him for business. It is also partly used by him for personal use, for pleasure. It is used by his family. Now, is that a retail purchase, or is it a purchase for a business?

Mr. PATMAN. Let me give you an illustration——

Mr. GOLDSBOROUGH. If the consumer were an individual, it would not make any difference if he used it in his business, as I see it.

Mr. MUNSON. It would be a little clearer if it were a store, where the car is used for the store business, and the store is not a retail buyer, but on Sundays the owner of the store will say "This is for my personal use; this is the car I am taking my family out in, for pleasure."

Mr. PATMAN. Suppose that there are two people doing business side by side, doing the same kind of business each year. One of them is incorporated, and the other is an individual. The incorporated concern you would make pay the full price for all of his delivery trucks and his automobiles, and therefore all that that corporation bought would be paid for at full price. But this individual, right aside of him, doing the same kind of business, and a competitor, would get the advantage under this bill of the 15-percent discount.

Mr. MUNSON. But the members of the corporation, when they go out and spend as consumers, would get the discount. The members of a partnership business, or of an incorporated business, in their capacity as consumers, would get the discount, but not in their capacity as a business, making purchases for business reasons.

Mr. PATMAN. Then they would be on their honor as to what they were going to use it for.

Mr. MUNSON. It is a little more than honor. It is their self-interest.

Mr. PATMAN. You could not afford to have enough agents to run down all of those transactions.

Mr. MUNSON. You would not have to. You must never forget, in discussing business trying to take advantage of the retail price discount, that these businesses are going to have their costs recovered in the sales to the ultimate consumers, aided by the retail price discount. They are not going to be so much concerned as they are now, because the market for their product is going to be immensely strengthened. Then——

Mr. PATMAN. And who can get a license under this bill? Suppose that the set-up is——

Mr. GOLDSBOROUGH. I think that he should be allowed to finish his answers.

Mr. PATMAN. He had finished his answer, had he not? If he had not finished, I beg his pardon. I will permit him to finish.

Mr. MUNSON. That is quite all right.

Mr. PATMAN. All right. Say that this law is passed. Somebody here in Washington has got to license all of these people. Are you going to pick out a few to license? Will you force all of this business into the hands of a few businessmen engaged in the retail business, or will you give everyone a license? How will you determine who shall and who shall not be licensed?

Mr. MUNSON. I would say that that was covered under section 402 of page 15.

Mr. PATMAN. What does that say?

Mr. MUNSON. That—

> The Secretary of the Treasury is authorized to make such rules and regulations as he may deem necessary to carry out the provisions of this Act.

Mr. PATMAN. In other words, in any town over 1,000 people, where there may be two or three grocery stores, if the Secretary of the Treasury decided that they did not need any more grocery stores, he would not allow anybody else to be licensed?

Mr. MUNSON. That does not follow. That is the sort of question I would say should be put up to an administrator.

Mr. PATMAN. Suppose that you were the administrator, and suppose that that question were put up to you? It would be just like it is with banks now; they will not permit another bank to be established.

Mr. MUNSON. The point here is that I am not an administrator.

Mr. GOLDSBOROUGH. You cannot find anything in the bill which would give the Secretary of the Treasury the power to decide the number of retail businesses to be established in any locality.

Mr. PATMAN. Are you willing for him to have that power?

Mr. MUNSON. I am not willing to have any more power granted to a central agency than is necessary.

Mr. PATMAN. I understood you to say, in answer to Mr. Goldsborough, that you would be willing to insert in the bill that that power should be in the Secretary of the Treasury.

Mr. MUNSON. Oh, no; that is in the bill now.

Mr. PATMAN. And you are willing for it to stay there?

Mr. MUNSON. I would say this, that that is a routine provision.

Mr. PATMAN. Routine? Do you mean as to who shall be allowed to run the business of this country is routine? I think that it is a very important question.

Mr. GOLDSBOROUGH. Do you find anything in the bill which directly or indirectly gives him any right to say whether or not a retail business shall be established or run anywhere?

Mr. MUNSON. No; of course not.

Mr. GOLDSBOROUGH. Well, then, say it. Mr. Patman says that there is something in the bill which gives the Secretary of the Treasury the right to decide whether a man shall run a retail business or not.

Mr. PATMAN. We will say that the bill does not permit him to do that, that he cannot pass upon that, that he just has to grant the license——

Mr. GOLDSBOROUGH. He has to grant the license to the retailer; yes, sir.

Mr. PATMAN. To anybody who wants to retail?

Mr. GOLDSBOROUGH. I do not see why not.

Mr. PATMAN. All right. We will pursue it from that angle.

Now, we have a million and a half retailers now, and of course this discount will be a great incentive for retailing, and suppose three or four more million people decide that they want to be retailers, and this butter-and-egg man gets himself a license up here and, instead of selling butter and eggs, he gets to selling automobiles, tractors, and everything else that he can collect 15 percent from the Government on. Don't you think you would have a rather confused condition existing in this country?

Mr. MUNSON. As I said before, every time you draw a picture like that, you are drawing a picture that would say that we could not administer the Social Security Act, that we could not administer any act passed. The details of administration are, necessarily, not part of the bill, but would be submitted to the appropriate departments of the Government with the statement "Here is the task of administration." And in the case of this particular bill, you would have something infinitely easier to administer than keeping track of 30 million citizens in connection with social security, and the like, and I think that we can have considerably more confidence in the talents of our administrators in the various departments of government than perhaps we seem to show, and these problems which are presented as insoluble problems do not seem to me to be anything more than the Government is already doing in connection with other bills.

Mr. PATMAN. Let us see. This includes barber shops, does it not?

Mr. MUNSON. It would include such barber shops as wished to get a contract to dispense the discount.

Mr. PATMAN. A 15-percent discount on a $1 bill would be 15 cents off, and I do not see why they would not come under it. There are 121,153 barber shops.

It includes beauty shops too, does it not?

Mr. MUNSON. Yes.

Mr. PATMAN. There are 4,302 of those.

It would include baths, such as Turkish baths, would it not?

Mr. MUNSON. Yes.

Mr. PATMAN. You have to pay $3 for that, and the Government would pay 45 cents of it.

It would include beauty parlors, of which there are 61,355.

Coming next to cleaning, dyeing, and pressing establishments, the Government would pay 15 percent of your pressing bill, too, would it not? There are 57,397 of those.

Then, funeral directors and embalmers. Does it include funeral directors?

Mr. MUNSON. I should say so.

Mr. PATMAN. That is a personal service.

Mr. MUNSON. I would say that that was retail.

Mr. PATMAN. There are 17,144 of those.

Fur repair and storage shops, 2,113. This would include furriers too, would it not?

Then laundries, not including power laundries, 16,826. Photographic studios, 10,402. Rug cleaning and repairing shops, 894.

It would include shoe-repair shops, shoe-shine parlors, would it not?

Mr. MUNSON. It might.

Mr. PATMAN. There are 61,046 of those.

Now, under business services, the bill would include disinfecting and exterminating service, and that would be included, would it not?

Mr. MUNSON. Yes—Well, you might complete the picture——

Mr. PATMAN. There are 596 of them.

You take all of these waiters; they have to rent their coats, full-dress suits, aprons, and so forth, and you would have the Government paying 15 percent on that.

Mr. MEEKS. How about the Congressmen who rent their dress suits?

Mr. **Patman**. That would be paid, too. If the Congressman had to pay 5 bucks for a dress suit some evening, the Government would pay 6 bits on it.

This includes real estate, doesn't it?

Mr. **Munson**. There is another problem to real estate.

Mr. **Patman**. There is no quarrel about that, that it includes real estate, and you say that there would be no incentive to cheat when it involved transactions of a couple thousand dollars. It might just as well apply to transactions involving hundreds of thousands of dollars. This would involve a sale of a home costing $100,000, would it not?

Mr. **Munson**. Well, what you——

Mr. **Patman**. I say, this bill would apply to the sale of a home costing $100,000?

Mr. **Munson**. You are quite right.

Mr. **Patman**. And there would be $15,000. Do you say that that is chicken feed? You say that there is no incentive to cheat. Suppose that that fellow decides to sell that home the next week. The Government would have to prove that he intended to defraud when probably he had some reason to change his mind, and if he is a retailer with a license to sell butter and eggs, he can sell that home again and make $15,000 on it.

This bill would include tourist camps and hospitals, and motorbus transportation, and I am just naming a few in addition to the food stores, which would include candy and confectionery stores, butter and egg stores, delicatessen stores, fruit stores and vegetable markets, grocery stores, meat markets, fish markets, bakeries, general stores, drygoods, departments stores, variety stores, the apparel group, men's and women's custom tailors, and if you got yourself a suit and you paid $100 for it, the Government pays $15 of that, would it not? Then it would include airplanes. Suppose that Mr. Goldsborough, if he gets this bill over, would want to fly over the country in an airplane and have a good time, like Lindbergh did. That airplane might cost $100,000, and wouldn't the Government pay 15 percent of that?

Mr. **Munson**. There may be something misleading in your constantly saying that the Government would pay it.

Mr. **Patman**. This interbank currency is a Government obligation, is it not?

Mr. **Munson**. No; it is not.

Mr. **Patman**. Whose obligation is it, then?

Mr. **Munson**. It is the obligation of the American people first to produce the goods and services upon which the interbank currency is based.

Mr. **Patman**. But whose obligation is this interbank currency? Somebody is responsible for it.

Mr. **Munson**. The American people.

Mr. **Patman**. You will agree with me on that much?

Mr. **Munson**. I agree that the responsibility of the American people is to produce the goods and services, and, having done that——

Mr. **Patman**. I know, but——

Mr. **Goldsborough**. I insist that he be allowed to answer your questions.

Mr. **Patman**. All right.

Mr. **Munson**. Well, the answer is complete except one single——

Mr. **Patman**. The answer is complete. That is a very vague answer.

Mr. MUNSON. But it is an answer I would like to fulfill a little later in detail, but I think we have not finished wrestling with this problem of fraud; that is, I would like to follow through along that line, which will not take much longer.

Mr. PATMAN. All right; go right ahead so far as I am concerned.

Of course, this includes all kinds of automobiles, motor accessories, tires and batteries, garages, filling stations, furniture and household dealers, floor coverings, household appliances and radio stores, lumber, hardware, farm implements, heating and plumbing, paint, glass, wall paper, electrical supplies, restaurants, cafeterias, lunchrooms and soda fountains, drugstores, bicycle shops, book stores, cigar stores, florists—and if you wanted to buy a $10 bouquet, the Government would pay $1.50 of it under this bill—fuel and ice, gifts, hay, grain and feed, farm and garden supplies, jewelry, luggage, news dealers, sporting goods, beer and liquor—and the Government would pay 15 percent of your liquor bill and beer bill—and you would have the second-hand stores, the pawn shops, and other stores.

Mr. REILLY. Doesn't your million and a half include all of those?

Mr. PATMAN. Not all of them. I am just talking about the ordinary retail store. As Major Angas says, it is impossible to define the term "retail store."

Mr. MUNSON. With a razor-sharp edge.

Mr. PATMAN. And I am putting some of this in the record to show you how impossible it would be to administer it. We know it would include liquor if this bill were passed, and let us assume that a man would go to his hotel, where he has a $10 room, and he buys $10 worth of liquor; the Government will pay $1.50 on the room and $1.50 on the liquor.

Mr. GOLDSBOROUGH. He could get a wholesale rate with that much money.

Mr. PATMAN. And it would not take very long, at that rate, for something to happen.

Mr. MUNSON. What we have had is a double picture. We have had a picture of the complexity of retail trade, which at the same time happens to be a picture of the enormous wealth of the country in real goods and services. The argument is that so complex is our retail trade, that it comprises so many items, that it really is unmanageable, that we cannot do anything about it. I think that that is a reductio ad absurdum. If we cannot do anything about it, how is it that we did do something about it?

Mr. PATMAN. They did not get 15 percent on that.

Mr. MUNSON. How is it that we have these many laws operating with a fairly high degree of administrative success?

Incidentally, the social security legislation is a taking from firms and individuals for the purpose of redistribution, and it lacks the favorable side of this bill, which is, so to speak, a giving of strength to business and to consumers, so that if social security as a taxation measure works, then a measure like this, which is an aid to the consumer and to business, ought to work with much less friction.

Mr. PATMAN. You are talking about social security. What about Oklahoma, where it is claimed there are people on the roll who never made application that they are supposed to be giving pensions to, and some of them are even dead? That is an example of how a law will be abused, and if the people will abuse a law for $15, what will they do in connection with a law for $15,000?

Mr. MUNSON. It happens to be an example that relates to my former remarks having to do with decreased incentive to fraud and having to do with legislation which on the one hand is unpopular in character, in that it takes from the people, and legislation that ought to be popular in character in that it added to purchasing power.

Mr. PATMAN. If you rent an apartment here in Washington, and pay $5,000 a year for it, how is that going to help the country if the Government pays $750 of it? How is that going to increase the consumption of goods and services?

Mr. MUNSON. Well, I should think the answer was quite clear. You cannot say that your business slump is very helpful to the Government or to the people. Now, if you revive business, it obviously means increased living conditions for the population.

I do want to cover two or three more points on fraud. There is the matter of price inflation. That has been brought up. We will call it profiteering, and, if you recall my testimony here last July, you may remember that in section 7 of that I dealt with that particular form of price inflation. That to me is the strongest point raised on the administrative side of this bill. There are very simple means available for meeting that, and they were suggested by me last July, and again suggested by Mr. Brougham a week or two ago. That is a specific form of inflation, and there is a specific device to meet it.

Then we were told, how can you distinguish between different degrees of bank runs, and won't the scheme be frustrated on that score? To begin with, the provision in the bill for the conversion in an emergency of interbank currency into cash is not a vital part of the bill, in my estimation.

Mr. PATMAN. You would be willing to strike that out?

Mr. MUNSON. Oh, yes.

Mr. PATMAN. What would you have left?

Mr. MUNSON. You would not need to put anything in its place, but in the examples given, of initiating mild runs on banks, we have been asked to believe that business would suddenly reverse its habit and want cash instead of going on doing a checking business. We have been asked to believe that cash is not coming into the bank at the same time it is going out. We are asked to believe that the bank would risk the penalties in this act for collusion under this scheme. We have to keep in mind those penalties matched against the possible gains, which I have been saying right along would be of little profit.

Finally there is to my mind a much more serious question and a question which this bill is not called on to solve, but which the administration of it would be called on to solve if the bill became law, and that is hostile action by the banking system, action of a sort designed to bring about a disastrous inflation, not in terms of the mechanism of the bill, but outside of it.

When we talk about inflation we have got to think as clearly as Major Angas, who said that the word for him had 22 meanings. We are apt to think of inflation as a blanket term, and we try to kill it with a shotgun. Actually inflation is specific in character, and it calls for specific measures against it.

Now, it would seem to me that some kind of board of strategy—it might be a Federal Credit Commission—would be engaged in the administration of this bill, in adopting measures to frustrate any hostile action by the banking system, but that arises outside of the terms of the bill.

Mr. WILLIAMS. What is inflation?

Mr. MUNSON. The general definition of inflation would be this, an increase of money accompanied by a rise in prices. You see, you have to have those two things. Sometimes money is increased and prices do not rise. It has to have those two features, more money and higher prices.

Mr. WILLIAMS. That is your conception of it?

Mr. MUNSON. That is the standard conception.

Mr. WILLIAMS. I understood you to say that it had 17 different meanings.

Mr. MUNSON. No. Major Angas said that the word for him had 22 different meanings. I am sorry that I have not the knowledge of the 22 meanings which Major Angas has.

Mr. WILLIAMS. It simply means a rise in prices and an increase in money?

Mr. MUNSON. Yes, sir; that is a good workable definition, but, you see, while that is a general description of inflation, the inflation can take various forms. Earlier I mentioned price inflation out of a profiteering. You can inflate profits, you see. That would be, I am sure, 1 of the 22 definitions that Major Angas had in mind.

Mr. WILLIAMS. It does not make any difference what causes it. It is simply a rise in prices——

Mr. MUNSON. Accompanied by a greater volume of money.

Mr. WILLIAMS. What relation does the velocity of money have in the system?

Mr. MUNSON. Well, to my mind the velocity of money theory is mostly a fallacy.

Mr. PATMAN. Velocity is a fallacy?

Mr. WILLIAMS. It does not mean anything whether the money turns over once or 10 times, you say?

Mr. MUNSON. The more money turn-over, the more velocity there is, but it does not increase the amount of money, no matter how many times you turn over a given amount.

Mr. WILLIAMS. No one contends that it increases the amount of money, but certainly everybody will contend that it does influence trade and prices.

Mr. MUNSON. I think what is meant by most people when they use the term is really velocity of short-term loans, the velocity with which short-term loans are reissued, but it means really new money.

Mr. WILLIAMS. It does not mean that to me at all. It simply means the number of times that that money is used in the circulation of money, whether it is currency or credit.

Mr. MUNSON. But the difficulty is that our money is coming out of the banking system in the form of money creating these new loans, and it is returning to the banking system to be canceled in repayment.

Mr. WILLIAMS. Suppose that we increased the volume of money, doubled it, as this bill contemplates, or more than doubled it. Where does the money go to?

Mr. MUNSON. The money goes to liquidate the debts of industrial society.

Mr. WILLIAMS. Where does it finally land?

Mr. MUNSON. It finally lands in a cancelation machine, the banking system.

Mr. WILLIAMS. It lands in the banking system?

Mr. MUNSON. Yes.

Mr. WILLIAMS. It goes back into the banks—that is a fact, is it not?

Mr. MUNSON. It goes back there to repay debts.

Mr. WILLIAMS. If instead of there being $6,000,000,000 in circulation, we doubled that and made it 12 billions, there would be only a short time when that would be right back in the banks and wind up as reserves in our system.

Mr. MUNSON. Not only as reserves; it winds up in liquidating the debt structure. You have an enormous brake on monetary expansion in the case of a bill like this, because you have a huge debt structure.

Mr. WILLIAMS. Suppose that I owed $1,000, and this bill were put into effect and I got a 15-percent discount on everything that I bought and I spent it all by reason of that discount in increased consumption of goods. How would I ever pay the $1,000 back?

Mr. MUNSON. You would not repay it by spending on consumption, but you would by producing and selling goods.

Mr. WILLIAMS. How do I pay it as an individual? It is my obligation.

Mr. MUNSON. You would have to be in business; you would have to be receiving a salary of some sort; you would have to get your money on the producing side, and with that you would repay your bank loan of $1,000, but you could not possibly do it as a consumer spending money.

Mr. WILLIAMS. In other words, you would increase the profit on the product.

Mr. MUNSON. You would probably increase the producer's rate of profit, the turn-over.

Mr. WILLIAMS. That would mean a rise in prices by the producer.

Mr. MUNSON. It would not necessarily. You see, the producer is first of all concerned in recovering his costs. There are many reasons why——

Mr. WILLIAMS. If he is going to pay up his obligation, he has to make an increased profit to do it, in addition to the cost.

Mr. MUNSON. In his judgment, when he made that loan, he figured a certain volume of business at a certain rate of profit would enable him in 3 months' time or 6 months, time, say, to repay it. Now, he falls down on that promise only, if he must catch a slump like the present one and he is not selling his goods. But if he runs into a good market, and his calculations have been reasonable, he then has recovered from the public the funds necessary to pay off his bank loan.

Mr. WILLIAMS. By increased business?

Mr. MUNSON. That is correct.

Mr. WILLIAMS. And without any additional profit?

Mr. MUNSON. No.

Mr. GOLDSBOROUGH. What you mean is that he would sell more articles at the same price and get a profit on each article, and if he sold more articles he would have more profit?

Mr. MUNSON. In amount; yes, sir.

Mr. WILLIAMS. Well, as he sold more products, of course his costs would increase, too?

Mr. MUNSON. It depends. Sometimes the unit cost goes down with increased business.

Mr. WILLIAMS. Sometimes it would, with mass production; I think we could all agree that it would go down sometimes, but you think that that would meet the entire problem?

Mr. MUNSON. Do you mean so far as cost recovery on the part of business is concerned?

Mr. WILLIAMS. Would it help him to pay off his debt? Your idea is that we would reach a condition when nobody would owe anybody anything?

Mr. MUNSON. It would take a very long time ever to reach that condition. My statement earlier had to do with a brake which operates automatically on any better time that was brought about, and that brake is the volume of existing debt to be paid off, which is a cancelation of money.

Mr. WILLIAMS. As I say, your idea is that this bill, if carried out to its ultimate conclusion, would result in a condition where nobody would owe anybody anything and we would have no occasion to borrow any money from a bank.

Mr. MUNSON. I would rather not take so long a view as that. I would rather say that this bill in its operations would enable business to sell at a profit with more ease than business can now, most business being near the line of insolvency, and it would produce what we call prosperity.

That is the short view and, I think, that is a sufficient view.

Mr. WILLIAMS. We never have reached that condition yet, have we?

Mr. MUNSON. Of real sound propserity?

Mr. WILLIAMS. Yes.

Mr. MUNSON. I do not think we ever have.

Mr. WILLIAMS. And we have never reached a condition, and never will, when everybody will be out of debt.

Mr. MUNSON. It is not so much, Mr. Williams, a case of being out of debt as of being able to repay debts. There is no objection to borrowing, but there is the trouble of repayment in a financial system which operates the way our present system does.

Mr. WILLIAMS. You are not opposed to the debt system, to the creation of debt?

Mr. MUNSON. No. I am not opposed to the debt system. I am opposed to money creation exclusively in the form of debt, you see.

Mr. WILLIAMS. Money is not created exclusively for debt, is it?

Mr. MUNSON. Practically all of it is.

Mr. WILLIAMS. Suppose that I go and deposit $1,000 in the bank, and get credit for it.

Mr. MUNSON. Yes; but you have not created that $1,000, since you are not a banker. You have got the $1,000 from somebody else, for services rendered. You have received $1,000, let us say, from a number of clients, but that is a very different process——

Mr. WILLIAMS. That is one of the processes.

Mr. MUNSON. But it is not a process of creating the money. You have only had money transferred to you which was already in existence, already been created by other people.

Mr. WILLIAMS. How much money is there in creation now? How much has been created in this country?

Mr. MUNSON. I could not give you the exact figures. At the present time there is, I belive, roughly about 6 billion dollars of cash and about from 33 to 35 billion dollars of bank-created money.

Mr. WILLIAMS. Do you mean by bank-created money simply when a man borrows from the bank and he is given credit for the amount of that, and he gives his obligation to pay it?

Mr. MUNSON. That is correct.

Mr. WILLIAMS. And it is secured by tangible assets?

Mr. MUNSON. That is correct.

Mr. WILLIAMS. That credit is secured, is it not?

Mr. MUNSON. That is right.

Mr. WILLIAMS. It is not created out of nothing, is it?

Mr. MUNSON. In a sense, it is.

Mr. WILLIAMS. In what sense?

Mr. MUNSON. In the sense that a number of notable economists have said it is—for instance, Dr. Moulton, the president of the Brookings Institution.

Mr. WILLIAMS. The mere fact that a number of them say so does not necessarily make it so.

Mr. MUNSON. It does not, but on the other hand, I think we can say that it is fairly indisputable today that banks, when they make loans, create new money. At least, it is so stated in the Encyclopedia Brittanica, and Dr. Moulton, whom I referred to a little while ago, in a college text book——

Mr. WILLIAMS. But they don't create it out of nothing, do they? They do not just reach up in the air and get it?

Mr. MUNSON. Mr. Hawtrey, who is a member of the Treasury Department of Great Britain, and who is known as an authority on central banking, says just those words, that banks create the means of payment out of nothing.

Mr. WILLIAMS. They do not any more make money out of nothing than the tailor makes a suit out of the cloth, do they?

Mr. MUNSON. In a sense, I would say they do.

Mr. WILLIAMS. And they do not any more make money out of nothing than a miller makes flour out of wheat?

Mr. MUNSON. That miller is in the physical world, and he does find there that you cannot make something out of nothing, but in the world of bookkeeping, you do. These are not my words, but they are the words of Mr. Hawtrey.

Mr. WILLIAMS. What do you think about it? Do you think that they just reach up out of the sky and pull it down, without anything in back of it at all?

Mr. MUNSON. When you say without anything in back of it, that is another question; but, so far as the technique of money creation by the banks is concerned, it is very often described by highly conservative economic authorities as creation out of nothing, but there is something in back of it. What is in back of it is ultimately what we call the real credit of the Nation, namely, its ability to produce and consume goods.

Mr. WILLIAMS. But there is in back of each loan from the bank, the individual responsibility of the borrower?

Mr. MUNSON. That has to do with the repayment of the loan, but it does not have to do with the creation of the loan.

Mr. WILLIAMS. That is the security that is back of it?

Mr. MUNSON. That is part of the security. The security back of it is really a very complex thing, and really it is the security of an entire Nation.

Mr. WILLIAMS. Back of each bank loan?

Mr. MUNSON. Yes, sir.

Mr. WILLIAMS. You do not mean to tell me that because my loan at the bank is not good, the Nation would make it good? If the assets of the individual bank were not good, the bank would fail, notwithstanding that the resources of the Nation are perfectly good.

Mr. MUNSON. That was not the drift of my argument. What I am really saying is that money and credit are only good in proportion to the society in which they circulate. That is, the credit of our Nation depends on the education of the people, our factory plants, our inheritance, our ability to turn out wealth, and it is a higher credit, a higher real credit than the credit of a savage tribe, which has no credit. To me, all of our banking business ultimately rests on the human factor, on natural resources, on productive ability, and if we cannot produce, if we reverted here in this country to the state of savagery, our real credit would decline and decline.

Mr. LUCE. Are you through, Mr. Williams?

Mr. WILLIAMS. Well, I will quit. I will yield.

Mr. LUCE. May I bring this down to a simpler illustration, in order to find out your judgment on the effect of your program?

I have a man working for me. I pay him about $7 a day, and he comes to me and says, "I want to buy something, and if you will let me have $70, I will work 10 days for nothing."

A debt is created. It is the core of all debt an agreement to do work under a contract.

Is it your judgment that the program which this bill contemplates will result in his not having to work those 10 days?

Mr. MUNSON. I do not see that the bill has anything to do with that, sir.

Mr. LUCE. But I understood you to say that this program will ultimately wipe out debt, and I want to know if it is going to save my man from carrying out his promise to work for me 10 days.

Mr. MUNSON. In the case of you and your man, to begin with, you are not a banker, and you are not creating any money in that transaction.

Mr. LUCE. I am trying to cut money out of this thing, because money is based upon work later.

Mr. MUNSON. A little more than that.

Mr. LUCE. When my man promises me that he will work for me 10 days for nothing, if I let him have $70, there is created the simplest form of all debt transactions. All of the theorizing and all of the philosophizing that you can produce cannot change that fact.

Mr. MUNSON. Yes; but this is an employer and employee relationship.

Mr. LUCE. He is selling me labor.

Mr. MUNSON. That is correct, but it is not the relation of a borrower to a bank.

Mr. LUCE. You muddle it up when you bring the bank into this illustration. I am purposely making it simple for the purpose of getting your thought.

Mr. MUNSON. But the situations are not comparable, for when you borrow money from a bank, you are borrowing it from an institution which specifically has the power of creating fresh purchasing power.

Mr. LUCE. That does not make any difference so far as my transaction is concerned. You gave me to understand that you contemplated wiping out all debt. All debts are simple illustrations of the fundamental thing that I have pointed out; that is, the basis of all debt is a promise to give production in return for temporary facilities.

Mr. MUNSON. Yes, and I think the record will show that my statement was a much more qualified statement than you have just described; that is, to begin with, I wanted to throw out the long view. I said that I am concerned more with the short view, which I call simply a revival of prosperity. Ultimately I was concerned to show the debt structure, as it exists now, operating against the fears that this bill will prove inflationary because your debt structure will put a brake on the new money coming in and liquidating costs.

Mr. GOLDSBOROUGH. Is there anything in this bill which will prevent one man from borrowing money from another, or from borrowing money from a bank?

Mr. MUNSON. No, there is not.

Mr. WILLIAMS. What is the difference whether you borrow from a bank or from an individual, so far as the debtor is concerned?

Mr. MUNSON. So far as the debtor is concerned, when it comes to repaying the debt, there is not any difference, but so far as society is concerned there is a big difference.

Mr. WILLIAMS. What is it?

Mr. MUNSON. The difference is that when a bank makes a loan, it increases the amount of new money, but when I or you make a loan, we cannot increase the quantity of money in any way. We merely take $10 which we got from somebody else and pass it on to somebody else, and we do not create 10 new dollars.

Mr. WILLIAMS. You get back to the proposition that you cannot have any extra money outside of what you have locked up in the vaults, a 100-percent reserve system, in fact. Isn't that what it leads to?

Mr. MUNSON. I myself do not get back to that, because I am not an advocate of the 100-percent reserve.

Mr. WILLIAMS. You are criticizing these loans from the banks, the system of borrowing money from the banks.

Mr. MUNSON. I did not assume to criticize it.

Mr. WILLIAMS. If you cannot borrow money from the banks or from somebody, you eliminate the debt system or borrowing system entirely.

Mr. MUNSON. You misunderstood me.

Mr. GOLDSBOROUGH. Is there anything in this bill which decreases the possibility of deposits in banks which the banks can loan?

Mr. MUNSON. None whatever. My position is certainly not that of the abolition of borrowing from the banks. Not at all. My position is that they have the exclusive right now to mint new money.

Mr. WILLIAMS. What would you do with it? You say that you are in favor of borrowing from them. How would you manage it?

Mr. MUNSON. I would do exactly what this bill prescribes. I would admit certain debt-free money along scientific lines into the hands of consumers, so that no longer would money creation be an exclusive and monopolistic practice. Then, with your strengthened market, of course your producers are going to go to the banks and borrow to expand production, to meet the increased demand that goes along just the same.

Mr. WILLIAMS. What would they borrow for?

Mr. MUNSON. I think they would borrow to increase their plants, in order to meet the increased demand brought about by the operation of this bill.

Mr. WILLIAMS. They can do that now, can they not? What would be the difference between the man who borrowed from the bank under that scheme and the man who borrows now?

Mr. MUNSON. There is now said to be a considerable reluctance to do that sort of borrowing, because the manufacturer does not foresee any rise in demand for some time. He is waiting to see if conditions won't get better.

Mr. WILLIAMS. You recognize the fact that there is plenty of money now, don't you, that they can borrow?

Mr. MUNSON. The plenty of money is not in the hands of the consumers.

Mr. LUCE. Right on that point, I want to go back to one of the stones you laid in your foundation, if I may, Mr. Williams——

Mr. WILLIAMS. Go right ahead.

Mr. LUCE. You laid down the theory that crime is due to a shortage of money, and you went on to speak of money stringency. Do I gather from that that you believe that if you increased the amount of money, crime would be lessened?

Mr. MUNSON. Yes, sir, I would say that.

Mr. LUCE. That is interesting.

Mr. GOLDSBOROUGH. May I say on this point that I think all sociologists agree that crime is the direct outgrowth of poverty. I do not think that there is any question about that.

Mr. LUCE. Yes, that has always been my judgment, and it leads me to the next question: How do you put any more money into the hands of the type of men you find before the police courts?

Mr. MUNSON. Do you mean what the provisions of this bill would do?

Mr. LUCE. Yes. You laid down the proposition that there is a scarcity of money—you said "money stringency," and you alleged that some poor devil in court who snatched a pocketbook would not have done it if he had had some money. How would this bill or any other bill put money into the hands of that poor devil?

Mr. MUNSON. The mechanism provided by this bill is a 15-percent discount, which is something like a 20-percent rise in purchasing power, which would in turn make more jobs available and which would in turn enable money to be distributed more throughout society.

Mr. LUCE. But you would still have the inefficient, you would still have the moron, and you would still have——

Mr. MUNSON. Of course.

Mr. LUCE. You would still have the fellow who could not render to society in service what society gives him. How will you get rid of that by any monetary bill? Do you mean a money stringency of the type that the Populists called for 55 years ago, or do you have some other conception of it?

Mr. MUNSON. I mean simply the inability of the whole population ever to claim its total production.

Mr. LUCE. Then you are not a cash inflationist?

Mr. MUNSON. Oh, no. You see, the problem that you have raised is a problem for the criminologist and for the humanitarian.

Mr. LUCE. Surely, but you are approaching it as an economist.

Mr. MUNSON. Yes.

Mr. LUCE. And it is only as an economist that I am interested in these things, and I am surprised at your statement that 90 percent of our crime is traceable to a shortage of money.

Mr. MUNSON. But when you go to the sociologist or to the criminologist, he traces crime, as I have said, and that is a standard figure, that 90 percent of it is for a financial motive. If you can succeed from the economic point of view in making that motive seem less important, you have begun to draw away the power of this drift to crime. You then put your criminologist in a position to do something more effective than he can now do.

Mr. GOLDSBOROUGH. Mr. Munson, let us get down to cases. There are two poor devils in the police court, ready for trial, each for petty larceny. One of them is a man who has been a bum for 30 years; he has peddled himself around the country with a little pack over his shoulder. He is a moron. The other individual who is in police court for petty larceny has not had a job for 4 months. He has a wife and four children. He has no fire. His children are crowding around his legs, begging for something to eat, and he goes out and steals a loaf of bread.

While you could not by the operation of this bill save the individual who is beyond reclamation, you could give employment to that individual who simply could not get a job. Isn't that all there is to it?

Mr. MUNSON. That is a very strong statement of it, but I would like to add that it is not only the crimes of the police court that we have been thinking about, but let us take embezzlements. It so happened that I once had to look over the records of something over 1,000 cases of embezzlement. It was extremely interesting, the conclusions which these researches led to. They found first that the people who embezzled had been trusted employees for periods of 10, 15, or 20 years, that they were intelligent people, that they were respected and honest people——

Mr. GOLDSBOROUGH (interposing). You mean naturally honest.

Mr. MUNSON. Yes; as good as I am, as good as the next man. Now, there had come into the lives of these people some crisis. Perhaps the wife was going to have a baby, or hospital expenses, or something like that, and they needed more money, and this firm which conducted this research was a bonding house, I believe, and they said that this is the composite picture: Perfectly respectable people, but a financial crisis came into their lives, and these men and women break down after 10, 15, or 20 years of loyal service, and they take some money from the firm, but they never called it taking; they simply looked at it as temporary borrowing, which they would replace when the crisis was over, and they were never able to replace it.

There are thousands of cases of misery of that sort which seem to result from the wear and tear of a terrific financial struggle continued over the years, and that sort of person is a little different type from the moron, or the criminal trained in the streets from boyhood, or the desperate, unbalanced character.

Mr. LUCE. I quite agree with what you have just said, and also with what Mr. Goldsborough said, and I did not mean to be put on record as saying that many such cases did not exist. A member of my family was a police-court judge, and I well know that that is many times the case.

Mr. PATMAN. Would you mind stating what your background and experience are as an economist?

Mr. MUNSON. As a matter of fact, I do not call myself an economist. I call myself an economic journalist.

Mr. PATMAN. You have never claimed to be an economist?

Mr. MUNSON. It is not my profession.

Mr. **Patman**. And you have not been trained along that line?

Mr. **Munson**. I have been trained as an economic journalist. Of course, we are using words exactly here. Mr. Stuart Chase is an economic journalist; he is not a professional economist, and yet Mr. Chase's views are part, very much so, of the economic thought of today.

Mr. **Patman**. So they have the same standing, so far as you are concerned, an economic journalist and an economist?

Mr. **Goldsborough**. It depends upon who he is.

Mr. **Munson**. It depends entirely on the person. I would say myself that the professional economist has cut a very sorry figure since the war.

Mr. **Patman**. Sometimes we have self-confessed economists. Some fellow accused me of being an economist, which of course I am not.

Mr. **Williams**. Did you ever see two of them that agreed? I refer to economists.

Mr. **Munson**. I would say that disagreement is very healthy in any science.

Mr. **Williams**. But they are all sure that they are right.

Mr. **Munson**. Well, the man who has done his best to reach the bottom of a subject ought some day to reach a conviction.

Mr. **Williams**. It has always been a mystery to me that men who make that a study reach opposite conclusions, and all of them are absolutely sure that they are right.

Mr. **Munson**. The purport of my introductory remarks could be summed up as follows, that the world has changed since the first World War. We are in a power age. Before that war, we were in a machine age.

Mr. **Williams**. But you have all of these economists today, and they are as far apart as they ever were.

Mr. **Munson**. Some are living in the pre-war days. There is a definite split between the old and the new economist, which has grown up since the first World War.

(After an informal discussion, off of the record, not on the merits of the bill:)

Mr. **Goldsborough**. We will adjourn until next Monday morning at 10:30 o'clock.

(Thereupon, at 12:30 p. m., an adjournment was taken until Monday morning, February 28, 1938, at 10:30 o'clock.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

MONDAY, FEBRUARY 28, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee this day met, Hon. Henry B. Steagall (chairman) presiding.

Other members present: Messrs. Goldsborough, Reilly, Williams, Spence, Farley, Ford, Brown, Patman, Transue, Luce, and Crawford.

The Chairman. The committee will come to order. Gentlemen, we have with us this morning Mr. Allan R. Brown, a New York customs attorney, who will discuss Mr. Goldsborough's bill.

You may proceed, Mr. Brown, and make a preliminary statement, if you desire.

STATEMENT OF ALLAN R. BROWN, ATTORNEY AT LAW, NEW YORK, N. Y.

Mr. Brown. Mr. Chairman, I am an attorney in New York. For 30 years I have been dealing with practical problems of finance, and also of employment, because to the businessman employment somehow or other is the most difficult item of expense that he has to deal with entering into cost. Since 1916 I have made a special study of monetary conditions. I was forced into it for practical reasons because of monetary eccentricities of the war period.

The bill now under consideration, H. R. 7188, has been of great interest to me both in itself and also in its relation to its predecessor, H. R. 9216, which was before the last Congress.

The Chairman. What bill was that?

Mr. Brown. That was the Goldsborough bill. It dealt with very much the same subject, but is somewhat changed in its present form.

This bill represents a great advance over our previous monetary thinking, in that it consciouslyconforms more closely to the realities of production and consumption, than anything else I know of, and it limits itself to that conformity.

After all, when we speak of reality, economically, we refer to the facts of production and consumption, real wealth, such as food, shelter, and clothing. Money, important as it is, is only important insofar as it is used as a means to distribute those realities, and it gives the opportunity to get the basic necessities and such comforts and luxuries as people are able to provide themselves with.

Now, today, if the committee will hear me for a short time, I want to speak of the ultimate purpose and effect of this bill, and its primary mechanism, the retail discount, rather than go into the details of the technique.

Sometimes we lose sight of the forest because of our meticulous inspection of the individual trees.

In thinking about this bill, I have had in mind three points that I want to bring to the attention of the committee.

In the first place, retail discount is not a stimulus to artificial activity. It is rather a release from a restraint on the normal processes of production and consumption.

In the second place, the retail discount is really a communal mutual insurance proposition, rendering it possible for the community to take advantage of the economies inherent in capacity production.

In the third place, which is really a corollary to what goes before, this bill eliminates the necessity for a struggle between different factions in the community. It depends upon the cooperation of all factions.

It is not a struggle for a scarcity, but a communal marketing of the abundance to which we are entitled.

On the first point, let me say this. A week or so ago President Roosevelt said:

> The productive power of our workers and our resources, if fully utilized, can provide and maintain a national income far above any levels we have yet reached.

This is unquestionably a true statement. Then why do we not do what we might do? We evidently are not doing what we might do. With one-third of our people ill-clad and ill-nourished and ill-housed, it is evident that we as a Nation are not doing what we might do.

I think that the main difficulty has been that we have divided ourselves into classes, each fighting to get for itself a larger share of the insufficiency which has been produced, a larger share of the existing production, which is an insufficiency and an inadequacy. Instead we ought all to get together—capital, industry, labor, and farm groups—to produce more, as the President has said we are able to do, so that all can have a sufficient share. It is the difference between fighting for a slice of a small cake or getting together and making a big cake, of which each can have a slice.

Now, I would like to speak of the way that the bill does this thing. It does not divide the Nation into factions. This is not a bill for the benefit of the farmer; it is not a bill for the benefit of labor; it is not a bill for the benefit of big business. It is a bill for the benefit of all of us, as consumers. That is what the retail discount does.

If we try to advantage one faction at the expense of another, we do not get anywhere. If wages are increased, that will immediately benefit the wage earner, but the increase must enter into costs and eventually even the wage earner is hit by the higher prices. You can increase the price of one commodity as compared with another and the producer of that commodity will be advantaged, but the community as a whole will suffer.

This bill does not increase money wages. It does not attempt to balance prices. But it lowers all prices to the consumer. That is precisely equivalent to an advance in real wages, not money wages. It is more equitable than an advantage which is limited to the wage earner, because it applies to us all as consumers. It must be remembered that considerably less than half of our population are recipients of money wages.

What is the real reason that we are not utilizing fully at the present time our productive powers, the power of our workers and our natural resources? The workingman wants to work and the industrialist wants to produce. Certainly we all want to consume.

As the President has said, we can produce what we need, and there is a potential market for full production, but there is a lack of effective demand because there is a lack of purchasing power.

By this I do not mean that there is a lack of money in general, money idle in the banks, let us say, but there is a lack of money in the pockets of the people who buy, of the mass of the people.

We must remember that all of the lower brackets, as we call them, buy 80 percent of our consumer goods. There must be something radically wrong with the financial system.

To ease the situation, the R. F. C. has recently been authorized, in recognition of this fact, to make more liberal loans to the small-business man, to extend credits to the small-business man. But the existence of the basic flaw is revealed by the fact that even the administrators of this scheme fear that it will not work, that there will not be a demand for loans. This is only natural. Why should there be? Why should a businessman borrow money to produce goods that he knows he cannot sell. That same objection applies to any scheme like inducement loans, as well as to these R. F. C. loans.

Now, Dr. H. S. Person, Secretary of the Frederick Taylor Society of New York City, in a recent address in Indianapolis before the American Society for the Advancement of Science, made a distinction between industrial capitalism and finance capitalism.

I know that there is such a distinction; I have met with that distinction many times in my experience.

Recently one of my friends who is the sales manager for a large and important corporation said that the members of his board of directors were almost all bankers or investment brokers, and they would often turn down a contract which would be advantageous to the company simply because they were on the short side of the market.

Dr. Person said flatly that finance capitalism did not give industrial capitalism the free rein necessary for the the maximum utilization of the developments that modern science has discovered. That was what the President referred to.

Dr. Person said that these developments, if the industrialist is left free, make it possible for us as a nation to supply all that we need and want.

Mr. Ford. Mr. Brown, you made a statement a few moments ago that I would like to ask you about. I understood you to state to the committee, in the course of your statement, that an industrial organization would reject an order solely on the ground that such an order would affect the price of that corporation's stock. Do you tell us that?

Mr. Brown. I am telling you that when an industrial organization is under the control of people who have, not the interests of the industry, but the interest of finance at heart.

Mr. Ford. Let us take General Motors, for instance. Say that General Motors has an order for 10,000 cars—you just referred to dealings on the stock exchange—suppose that they had just received an order for 10,000 cars over and above their normal production, do you mean to tell this committee that they would reject that order because that might affect the price of their stock on the stock exchange? Do you mean to say they would refuse that order on that account?

Mr. Brown. I know that such a thing has been done.

The CHAIRMAN. Do you know that has been done?

Mr. BROWN. Yes.

Mr. FORD. What is your background?

Mr. BROWN. I have been an attorney for 30 years, conservatively.

Mr. FORD. For corporations?

Mr. BROWN. Partly for corporations, but mostly for importers.

Mr. FORD. Do you mean to tell this committee—you made a statement that seems to me to be outside of the scope of the Goldsborough bill—do you mean to tell this committee that a nationally ramified corporation would refuse an order for a great quantity of their product simply and solely for the purpose of affecting the price of that stock on the exchange?

Mr. BROWN. I say that can be done and has been done.

Mr. FORD. Has it been done?

Mr. BROWN. It has been done.

Mr. FORD. On a great scale?

Mr. BROWN. That I cannot say.

Mr. FORD. How do you know that the refusal of such an order was merely for the purpose of affecting the price of stock on the stock exchange?

Mr. BROWN. It is impossible to go into motives; that is why it is impossible to prove anything.

Mr. FORD. Then why say something you cannot prove, because this committee deals with matters that affect the whole economic and monetary structure of the United States. Why make such a statement as that to this committee?

Mr. BROWN. I do not say that industry is running in the main on that basis, but I do say that this has been done and can be done.

Mr. GOLDSBOROUGH. I am going to ask that Mr. Brown be allowed to complete his statement, because if he does complete his statement it will throw an entirely different light on this question, and his statement, in my opinion, will be extremely valuable to the committee.

The CHAIRMAN. I am sure that is agreeable to Mr. Ford.

Mr. FORD. That statement was made, and I just wanted to clarify it at this point.

The CHAIRMAN. You may proceed, Mr. Brown.

Mr. BROWN. I made the statement from my own personal knowledge, rather in connection with the attitude that Dr. Person has taken.

The CHAIRMAN. You may proceed.

Mr. BROWN. I did not make a point of it, because I do not believe it is necessary to go as far as Dr. Person has gone.

He said, to use his own words, that the attitude of finance capitalism as masters instead of servants of industry—

> leads to disappearance in the central market of automatic adjustments, to price controls and rigidity in the price structure, maldistribution of the social income, impaired purchasing power and similar obstacles to realization of the benefits of progressive technology.

Quite without our knowing it finance capitalism has obtained complete control over industrial capitalism, the capitalism that runs factories and makes the goods, and for its own advantage wants to supply them to the people. As Dr. Person said, financial capitalism—

> guards industrial capitalism as jealously as the planter guarded his slaves and for the same reason.

It is not necessary to go as far as Dr. Person has gone. It is not necessary to visualize the sinister figure of a finance capitalist throttling industry for his own pleasure. It is not even necessary to go into the question whether or not under our present system banks create money. The unassailable fact is that banks lend money to producers. They cannot, by the very nature of their business, lend money to consumers.

Naturally, also, their loans to producers are limited, not by what the consumer wants and what the producer can produce, but the bank's loans are limited by what the producer can sell. Any banker will say that he cannot go any further than this without going into bankruptcy himself.

The banker is quite right. It is unnecessary to introduce any sinister motives. The plain fact of the matter is that our money system has never been geared to the modern system of mass production. That deficiency is what this bill supplies.

The former bill, in words, abolished the fractional reserve system. The present bill does not do that, but it supplements the money which the banker loans, whether or not he creates the money for the loan, by costless debt-free money which is based upon no estimate, but which is based upon what the consumer actually buys. It exactly matches goods with dollars.

This is the only way to avoid either inflation or deflation. The issuance is based not upon an estimate, but a fact, the fact of production and consumption.

A residuary supply of money is issued which exactly balances consumptive requirements. I feel very sure that when the possibility of such issuance exists very little actual issuance will be needed.

In other words, the producer knows that there will be a market for his goods. It is in this way that the natural phenomena of production and consumption will have been freed from a restraint which is inherent in the money system of the horse-and-buggy age and which it is unnecessary to lay to evil motives.

I will not go into the question of how a retail discount operates. I know that I am speaking at the end of the hearings on this bill.

But I can say that putting money into existence after the goods have been sold, or upon the sale of the goods, is obviously a more direct way of dealing with the problem with which we are confronted, the problem of insufficient purchasing power, than building roads or battleships or other public works, or compiling guide books to cities, or raising wages to restricting production, or offering inducement loans, or any other method which has been suggested.

Now, as to the second point. The retail discount is in accord with the real conditions of mass production. Let me explain further. It is a truism that in the long run we cannot consume more than we can produce. To state the same proposition backward, whatever we consume we must pay the actual cost of producing the same.

Now, the answer is that we can reduce the price of each article by production in quantity, production in capacity. Everyone knows that if industry is operated at 30 percent capacity the cost of each article produced will be greater than if we were operating at full capacity.

This is undoubtedly the basis for President Roosevelt's plea to business to produce at capacity; that businessmen can produce the goods that we need and sell them as if they were producing for our capacity, even if immediate profits are not in sight. If production is at capacity, of course, employment in the Nation will be increased and of course at the same time it will be possible to lower costs and prices.

Something of this sort has been done by individuals before. There is one man I have in mind who at one time increased wages to an unprecedented degree, and at the same time he reduced prices, and he sold at a loss, or at least was selling without an appreciable profit, or any rate with practically no profit. By that means he built up a market and induced purchases so that ultimately and finally he made a great deal of money.

Now, of course, it is not every man who can do that. It is not every man who has the background of financial backing to enable him to do that.

I consider that this retail discount is practically an insurance scheme; it makes possible the communal enjoyment of the economies of mass production, without any individual taking a risk. It is really an actuarial method.

No one can tell whether this business or that business will be prosperous. There may be bad management, bad judgment, or a change in public taste in regard to a particular commodity which a particular business produces.

But we do know that the community, as a whole, can consume everything that our present capacity permits us to produce. There may be a few exceptions, although I doubt it.

If there are such exceptions, the surplus goods produced will be a real surplus, an unwanted surplus, not an unpurchasable surplus. Such goods can be used to purchase abroad the things we cannot produce here, at least on an economical basis. I will not go into that now, but I say that merely by the way.

The point is that, generally speaking, the Nation is at least justified in assuming that, on the whole, the community, if permitted, will consume everything that is produced at capacity. There is no risk here in general, and the risk of a failure of an individual business is absorbed by the general prosperity.

Now, the cost of the premium for this insurance is merely the cost of administering the retail discount, and this is very small as compared with the cost that the community has been put to.

The real prosperity of a nation is not determined by its monetary income; it is determined by the amount of real wealth which it consumes.

The retail discount is a plan for securing at the present time the economies of full production by the issuance of credits in a manner calculated to produce such full production and to stimulate still further production where needed. This will, of course, help not only the consumer goods industry, but also the heavy goods industries, and this is done by the mutual cooperation of the whole community in a way that no individual can afford.

Now, there is another point of view. The banker, when he makes a loan for production, has to not only consider whether the manufacturer can produce the goods and whether the consumer wants the goods, but he has to consider whether the consumer will be able to buy the goods.

Now, he has today an impossible task, because he has to estimate this for a particular business. Under the retail discount that difficulty is avoided because the retail discount comes to this determination not by way of an estimate, but by way of the actual goods sold. The credits are issued after, as, when, and if the goods are sold.

Now, on the third point, that is obviously a corollary to what has already been said. The retail discount plan is positive and constructive rather than negative and destructive. It avoids any necessity for the conflict between labor and capital, which is as costly as any war, not only to the community at large, but to labor itself.

What we call by the name of bargaining now is really a war of desperation with the odds always against labor. Just as it has been said that no war, however successful, ever pays for itself.

Labor may force higher money wages by strikes, but anything that they gain must eventually be lost in rising prices.

The retail discount cures this situation in a twofold manner. From the point of view of the laborer it is a raise in real wages, that is not money wages. From the point of view of the consumer, the necessary costs of labor as well as all other costs of current consumption are figured into the prices which the bill makes it possible for the consumers to pay.

On the whole, of course, the cost of production is consumption. What is used in the process of production is both in the way of raw materials, human energy, and the real wealth actually employed in supporting the producers and their dependents. This cost cannot be avoided, of course, and the bill does not attempt to avoid it. What the bill does is to avoid the unnecessary costs incident to partial and inadequate production.

At the same time, the bill will avoid the conflict between this business and that business, let us say, big business and little business. The bill issues the marginal credit not to the producer but to the consumer. Therefore, in the last analysis, the stability of a business will be determined not by its size or its financial backing, but to the degree in which it furnishes to the public wanted goods or services. Thus the public also will not have to take what it offers to it, but can choose what it wants. At the present time the public has to take what is offered to it by the survivor in the financial struggle.

Now, in closing, I want to speak of some of the objections which have been made to the retail discount plan.

One of those objections is as to the cost of handling the retail sales vouchers. The cost of handling retail sales vouchers by banking institutions would be very small as compared with the loss in well being and security which the public has already paid without securing the advantages of full production.

In 1929, according to one method of computation, we had a monetary income of about 90 billion dollars. On other, later years we have received one-third of that, or one-half of it, or two-thirds of it, in various years. This represented on the whole a corresponding reduction in the consumption of actual wealth, or real income, as I have previously defined.

The cost of administering the retail-discount plan would not be anything like that; in fact, it would be negligible. The plan would be self-liquidating.

I well remember, when a boy, that the banks were worrying about the cost of the growing checking system. But that has paid for itself.

Nothing has come of that fear of the banks, and I am very sure that in the case of the retail-discount plan the retailer would be very glad to pay the prescribed service charge to the banks, if the amount of his transactions can be increased twice or threefold, perhaps.

It seems to me it is entirely without foundation to say that the retail-discount plan would not change the existing trend of investments from bonds to loans to businessmen. When the main interest of the country is in current production and consumption rather than a futile attempt to conserve the monetary resources of individuals, that activity cannot fail to be reflected in the character of loans which are being made; it cannot fail to reflect the current activity. Even if this were not true the overindulgence in long-term investments would no longer affect the purchasing power of the community. In fact, I think that is one of the favorable features of the bill.

Now, the suggestion has been made that this plan might lead to sinister personal relationships between Government employees and favored private citizens. This is not true in the case of the retail discount because the credits contemplated to be issued are available universally. They are granted automatically to all, without distinction.

The suggestion of political partiality arises from a misunderstanding of the plan. On the other hand, the plan suggests that a loan to a particular producer would in its essence involve great difficulties in determining the character and choice of the enterprise to be helped and would afford the greatest temptation to partiality.

The suggestion has been made that there should be no other monetary agency than the Federal Reserve Board. But that question is not inherent in the plan. That is not an inherent difficulty of the plan.

The functions of the National Credit Commission as proposed as quite distinct from those of the Federal Reserve Board. The question of their exact relationship is a matter of administrative detail. If, in the future, it seemed advantageous to merge the two agencies, this can easily be done. The sole necessity is that the retail discount plan shall automatically reflect the actual facts of production and consumption.

The automatic operation of the retail discount is one of its prime features. It is incorrect to say that the plan represents a managed currency. That is just what it is not.

Trade cycles and depressions are caused by the management of money for itself alone, ignoring the economic needs of the people. The retail discount is not a form of management, but it is a removal of the distortion of the previous management, so that without management our money is left free to follow and serve in a natural way the facts of production and consumption, and so conform to the economic needs of the people.

Mr. **Crawford.** Mr. Brown, for the purpose of clearing the record at least, I understood the gentleman from California (Mr. Ford) in presenting a question to you to mention specifically a certain automobile manufacturing concern.

I think your answer was directed in such a manner that it hangs that burden on their necks. You did not mean it that way, did you?

Mr. **Brown.** I did not, and perhaps that caused the trouble. I do not think I mentioned an automobile manufacturer; if I did, that should be stricken from the record.

Mr. **Crawford**. That is what I wanted to clear up. The gentleman from California (Mr. Ford) mentioned a certain concern, and your answer was made in such a way that the casual reader of the record would interpret your answer as meaning to refer to that concern, while you did not mean it that way.

Mr. **Brown**. No; I did not. What I mean is this. The managers of a particular business, whether they are acting in favor of the producer of that business or not, have to consider the finances of that business rather than the industry of the community as a whole, and in very many cases they consider dollars as a part of the business, that is, the finances rather than the industry.

Mr. **Crawford**. I might say, in support of that, that I have witnessed cases like that at numerous times in the last 15 years.

Mr. **Brown**. I did not mean to refer to anyone in particular, or to rouse any question. But that is a matter I have known about for 30 years.

A friend of mine is in the lumber business and he owns 97 percent of the stock but he has never been able to make himself more than one director, and there are about six other directors holding 3 percent of the stock.

Mr. **Transue**. Will you amplify that a little bit, and explain, briefly, how that is done.

Mr. **Brown**. I can explain how that is done. That is done in many different ways. Suppose that the constitution of a corporation provides for the election of five directors. Now, here is a man who may spend much of his time abroad and he does not have the facility for gathering proxies that the others do. The other directors, who have only enough stock to qualify them as directors, make an active, shall I say political, campaign to have certain officers elected.

Now, all I meant to say was that under such circumstances one of those directors, who is managing the policy of the company, can easily make himself in control of the stock of the company in between elections, so his personal interests are directly contrary to those of the real interests of the company in question.

Mr. **Luce**. May I ask Mr. Brown if I state the gist of this program correctly when I say that it is a program under which the Government assumes a contingent liability up to 10 billion dollars for the sake of the general welfare of business and commerce?

Mr. **Brown**. Yes, to the extent of 10 billion dollars it is willing to buy a chance on the Nation; that is what I think.

Mr. **Luce**. While tke number of bank failures has been happily reduced, there are still bank failures from time to time.

In the case of a bank failure, if a bank has in its possession $100,000 of interbank currency, the Federal Government will pay the receiver $100,000?

Mr. **Brown**. I do not think it would.

Mr. **Luce**. That is in the assets of the bank?

Mr. **Brown**. Yes.

Mr. **Luce**. How will the receiver turn those assets into cash?

Mr. **Brown**. It seems to me that the indebtedness of the bank would be to other banks as well as to the public, and the other banks would have to take those proportionately, just as in the case of a clearing-house transaction.

Mr. **Luce**. There is nothing in the bill of that purport?

Mr. Brown. No; as I remember, the bill does not refer to that situation at all. If that is necessary, it can and should be inserted in the bill.

Mr. Luce. Why should the other banks have to pay out for this thing? This money, or these certificates, are guaranteed by the United States Government. You cannot pass the guarantee on to one of the banks.

Mr. Brown. I have not thought of that situation of a bank failure at all. I would have to take some time to consider it, because my mind works so slowly.

But I do not see why the other banks would be worse off if they accepted the currency in the clearing house transaction under the bill.

Mr. Luce. Somebody loses money in that case.

What I had in mind was that after the passage of this bill, if it is passed, unless some other provision were made, it would bring upon the Federal Government the necessity of making an appropriation each year of the amount of the interbank currency held by any of those banks. Therefore, there is a liability that may, to some extent, whether large or small, require an appropriation by the Federal Government?

Mr. Brown. I think that is an item that the committee should consider very carefully.

Mr. Goldsborough. I think Mr. Luce is correct in stating that under the provisions of the bill in case a bank gets into trouble, it would be entitled to real money in place of interbank currency with which to pay depositors in case of a run on the bank, or to pay depositors in the case of a bank failure.

But there is one phase which may have been overlooked.

If this interbank currency were in operation so as to maintain sales at retail that should go through the whole industrial system, how would you have any bank failures, unless there were extremely poor management or defalcations? How would it be possible to have bank failures?

Mr. Brown. Well, in times of prosperity you would not have bank failures at all. But I suppose there is a possibility that should always be considered, and it might be——

Mr. Goldsborough (interposing). Let me interrupt you at that point. If this retail discount were active and in such operation as to expand production to meet consumption constantly, how could there be anything but a fair prosperity at all times?

Mr. Brown. There could not be anything but fair prosperity.

Mr. Luce. If I may interpose there, let me say this. You have been speaking of the causes of bank failures. They sometimes come about through the ruin of a town or a city, or by the change in fashions. That is one illustration.

I know, for instance, in the city of Worcester we used to have a prosperous corset business. Of course, the fashion changed in that regard and killed the corset business. That is only a trivial matter in proportion to the great interests involved here.

But bank failures chiefly come about through rash loans. We had four trust companies in my own locality that went on the rocks because they had made bad loans in the financing of apartment houses, which was the chief reason why I objected to the recent housing bill.

It is by no means the fact, in my judgment, that the continuance of a bank is so closely allied to general prosperity as to put an end to bank failures.

Mr. GOLDSBOROUGH. I do not believe it would, but it could reduce them so that it would include only inefficiently managed banks, and banks where there are defalcations.

Mr. LUCE. As long as I understand the Government may be exposed to the necessity of making appropriations, that the contingent liability exists, that is all I wanted to develop.

Mr. GOLDSBOROUGH. I do not concede that myself.

Mr. LUCE. Where is the flaw in it?

Mr. GOLDSBOROUGH. The flaw in it is that in the conception of this bill the retail discount would not be used except for increased production, and therefore it will be self-supporting. That is the theory.

Mr. LUCE. I understand that is the theory, that is why I said, for the sake of the general welfare. But that does not destroy the fact that the Government does assume a contingent liability of 10 billion dollars.

Mr. GOLDSBOROUGH. But the liability under the bill would be paid by Treasury notes, not by appropriations, and not by taxation, unless the retail discount liability became so large that it was necessary to resort to taxation.

Mr. LUCE. Now, you have gotten me far beyond my depth. We are now running on the theory of an irredeemable paper currency, for the first time in history, I think. I do not remember any previous case where irredeemable paper did not produce cash.

If we are to continue with that theory, that everything may be irredeemable, I will have to learn my economics over again.

Mr. GOLDSBOROUGH. I do not think I made that contention.

Mr. LUCE. I thought that was the substance of your contention, that in view of the increased prosperity there never will be any demand for redemption.

Mr. GOLDSBOROUGH. No; my statement was this, or I meant this. My statement was that the increase in money would be matched by an increase in production, and that therefore there would be no inflation; that the increased consumption, due to the retail discount and the fact that the retail discount would always be available when a slump in business started, would tend to prevent, and would prevent, a depression, and that that being so, banks would not fail for any reason except an inherent weakness in the bank itself, not because of any general condition; and that being so, since most banks are well managed, there would be very seldom any substantial bank failures.

If there were bank failures this interbank currency would be translated into Treasury notes and would be available to cover the losses on this interbank currency, and that unless there were great demands for interbank currency it would probably be unnecessary to resort to taxation in order to keep the amount of interbank currency within the limits of 10 billion dollars. That is what I was trying to say.

My opinion is exactly like Mr. Brown's. I think that when production finds out that it has underneath it this continuous cushion which can be made available at any time, it will lose its fear, and that we will have little use for the discount.

That is my feeling about it. I do not think it will be necessary to call upon the discount.

Mr. LUCE. Well, I do not contest that at all, sir. I am merely trying to make clear myself where the ultimate redemption of the interbank currency will fall.

Mr. **Goldsborough**. Yes, of course; if it is necessary there is no question that it will have to fall upon taxation.

Mr. **Brown**. Yes.

Mr. **Luce**. Now, the contention has been made by you and others in the consideration of this bill that the amount of possible taxation which can fall upon society by the operation of this bill will be very small in comparison to the increased production and consumption which society will get by virtue of its operation.

Mr. **Brown**. Yes.

Mr. **Transue**. Mr. Goldsborough, there is one question I would like to ask some time. At some place the interbank currency would have to be redeemed; is that right or not? That is, this money that would be put into interbank currency in the banks is redeemable at some time in the future, or would that always be in the banks as interbank currency?

Mr. **Goldsborough**. Of course, Mr. Transue, you are asking me?

Mr. **Transue**. Yes, sir.

Mr. **Goldsborough**. I do not know whether you ought to take Mr. Brown's time by asking questions of me.

Mr. **Transue**. I would like an answer from you or Mr. Brown, either one. I have been seeking an answer to that question.

Mr. **Goldsborough**. That is a matter I am going to take up when I take the matter up with the committee again, but if you have no objection, Mr. Brown, I will be very glad to ask the question.

Mr. **Brown**. Yes, sir; all right.

Mr. **Goldsborough**. The theory of this bill is that this 10 billion dollars would be an initial fund available to be drawn upon for retail discounts, and the proponents of the bill feel that it will never be necessary to increase that amount, because they believe it will constitute revolving money. They believe that the banks from time to time, under the provisions of the bill will be required by the Treasury to call in this interbank currency because of rising prices, and that, therefore, not only will interbank currency be put into the market, but it will also be taken out; that it will not be necessary to increase the amount of interbank currency available above $10,000,000,000. So that, that $10,000,000,000 will be the only credit which will ever have to be set up by the Federal Government. If the interbank currency were to be used more than we anticipate and if, as a matter of fact, it was not called in as rapidly as it goes out, and the Federal Government thought that that $10,000,000,000 of interbank currency should not be increased it would then certainly be necessary for taxation to redeem a part of that. There is no question about that.

Mr. **Transue**. It would be withdrawn at times, when prosperity increased?

Mr. **Goldsborough**. Yes.

Mr. **Transue**. When it was withdrawn from the banks, and the banks have their own money in this interbank currency they would get real money for their interbank currency?

Mr. **Goldsborough**. Not under this bill; they would get credit on the books of the creditors.

Mr. **Transue**. It would amount to the same thing, as far as they are concerned?

Mr. **Goldsborough**. It would amount to the same thing, yes, sir.

Mr. **Transue**. Otherwise the banks would not be interested in this proposition at all?

Mr. Goldsborough. That is right.

Mr. Reilly. Mr. Chairman?

Mr. Goldsborough. Mr. Reilly.

Mr. Reilly. But in your judgment, what institution is responsible for the ultimate payment of the interbank currency?

Mr. Brown. I think the Nation as a representative of the people. All credit, eventually, must be based on the power of the people to purchase and consume. At the present time the banks use that basis of credit as far as they can, under the financial restrictions under which they operate. This is the use of that public credit by the Government for the same purposes that the banks now use it. The only difference is that the Government has the advantage of not proceeding in a particular case, but, in general. That we know is the sound way to do it. No insurance company can say when you or I will die, but they can say almost to the day when all individuals of our health and our age will die.

Mr. Reilly. Assuming under this bill, if it should become law, that $10,000,000,000 of interbank currency were issued.

Mr. Brown. Yes.

Mr. Reilly. Would not the Government have $10,000,000,000 more debt?

Mr. Brown. $10,000,000,000 debt?

Mr. Reilly. Ten billion more debt; we would have a bonded debt, an interbank currency debt.

Mr. Brown. I do not think that there would be any debt for that interbank currency as I read the bill.

Mr. Reilly. As you read the bill the Government would not be responsible at all for this interbank currency, is that my understanding?

Mr. Brown. I think the Government is responsible for it, but the bill makes it just as good as money for the original requirements of the bank. Take a $5 note. How is that to be redeemed?

Mr. Reilly. But the interbank currency cannot be used as money except between the banks and for reserves. The banks have phoney money when they get interbank currency.

Mr. Brown. I would not call it phoney money when they can loan dollar for dollar on it.

Mr. Reilly. But they cannot loan it.

Mr. Brown. But they can loan on it dollar for dollar.

Mr. Reilly. Only as they use it for reserves or release other money for your loaning purposes. Now, this bill provides that the banks may pay their taxes off in bank currency?

Mr. Brown. Yes.

Mr. Reilly. So, that would constitute an annual drain on the Treasury, would it not?

Mr. Brown. Yes; it would.

Mr. Reilly. Now, in 1927, 1928, and 1929, we had hundreds of bank failures at the very peak of our prosperity?

Mr. Brown. Yes.

Mr. Reilly. Are we not liable to have bank failures right along?

Mr. Brown. No; I do not think so. The reason we had bank failures at the peak of our prosperity was that it was always possible for the money of the community to be destroyed, that caused the reversal, just the possibility of that. Now that possibility is removed.

Mr. REILLY. Well, the records show that a great many of the bank failures were due to what is called inside jobs, and of the banks that are failing now are many of them due to a failure of the banks to realize their responsibility to their depositors?

Mr. BROWN. Yes.

Mr. REILLY. Now, Mr. Brown, what assurance would we have, or would anybody have that if $10,000,000,000 of discount interbank currency had been issued that all of that would have gone into the purchase of goods?

Mr. BROWN. To my mind the assurance would lie in the fact that the issuance of the credit is only made after the actual purchase of an article for consumption.

Mr. REILLY. Suppose Mr. Goldsborough were to buy an automobile for $1,500, and get a 15-percent discount, have you any assurance that he is going to expend that 15 percent extra beyond the amount he would have spent if he did not get any discount on that automobile?

Mr. BROWN. Well, he might not have been able to buy an automobile at all if he did not get the 15-percent discount.

Mr. REILLY. Do you think there are many citizens who could not or would not buy an automobile if they did not get that 15-percent discount?

Mr. BROWN. We can only use the automobile as an incident, but by and large the currency of the country, the actual cash turns over 40 times to 47 times a year, or something of that sort. It is used by the lower brackets who are paid salaries, and the money is turned right in to the grocers, and other furnishers of consumers' goods, and that shows that the lower brackets are not 2 weeks away from starvation. Now, if there were a 15 percent discount I am very sure that that would not curtail, but would increase their purchases. I do not know about Mr. Goldsborough's psychology, but by and large the 15 percent would be used for more purchases.

Mr. REILLY. Well, with 50 million people having deposits in banks, evidently they are living as they want to live. Will these people increase their purchases by 15 percent if they get that discount at the counters of trade?

Mr. BROWN. I think that they will, because I know that many of the deposits in banks are not put there because the individual does not want to purchase merchandise, but they are put there for the purpose of safety, a thing that we ought to get away from. I do not know if it can be worked out in 10 years or 20 years, but there should be a system so that nobody needs to put that personal savings in the bank because of terror, thinking if he dies, what would happen to his wife, and how his children will be educated, and so forth. I believe that savings today represent in 90 percent of the cases, fear of the future, rather than an unwillingness to consume further.

Mr. REILLY. In other words, they are saving for a rainy day?

Mr. BROWN. Yes.

Mr. REILLY. Would there not be a tendency to put that 15 percent in the rainy-day fund too?

Mr. BROWN. That is a matter of psychology, and no man can foresee that, but it seems to me when there is a prospect of a free economy such as is afforded by this bill that people would not further increase, at least, the proportion of their savings.

Mr. REILLY. You would have no fear of the possibility of fraud on the Government through the workings of this bill?

Mr. **Brown**. I do not think that the bill offers unusual possibilities of fraud, any more than conditions in income tax. It is a tax bill in reverse, really, and why there should be more fraud in this bill than in the other cases of tax bills, I cannot see.

Mr. **Reilly**. In the tax matters we do not have so many people to deal with. You would have 130,000,000 or 120,000,000 people in this bill to check up on, would you not?

Mr. **Brown**. No; I do not think there is any necessity of checking up on every individual purchaser. It would be necessary to check up on every retail establishment, just is it is in the case of income taxes today.

Mr. **Reilly**. Well, then, would the Treasury of the United States take a statement of every businessman as to how much discount he gave?

Mr. **Brown**. No; I say that would have to be checked up just as in the case of income taxes today.

Mr. **Reilly**. There are from one million to a million and a half business institutions in this country that will be licensed. You would have to check up on those people, would you not?

Mr. **Brown**. There would not be nearly as many to check up on as they check up on now. It could be done at the same time, and it will have to be done at the same time that the field agents check the business of the company for income tax purposes.

Mr. **Reilly**. We only have a very limited number, compared to the population, who pay income taxes, and they are 3 years behind in their check-ups now or 4 years behind. When would they get up, and how could they get up in checking up on all of these retail stores?

Mr. **Goldsborough**. How about sales taxes, which are universal? They have a retail sales tax in New York.

Mr. **Reilly**. Now, many of the sales taxes are collected right at the time of the sale, but the point in this situation is you have a very great incentive to fraud. You have had a recent example out in Oklahoma where they have defrauded the Government of $700,000 on old-age pensions.

Mr. **Goldsborough**. They have not done that in Wisconsin?

Mr. **Reilly**. No, Wisconsin is a very good State, and we do not do those things up there in Wisconsin.

Mr. **Crawford**. Mr. Chairman.

Mr. **Goldsborough**. Mr. Crawford.

Mr. **Crawford**. Mr. Brown, you have not any quarrel with the conservative banker who operates his bank so as to be ready to meet the withdrawal demands of his customers?

Mr. **Brown**. No.

Mr. **Crawford**. The point I understand you were trying to make was to suggest to us that there is a means of economy in the monetary system which would bring the handling of money, financing, and the medium of exchange around to where it somewhat coordinates and synchronizes with the production of goods, first, the consumer's demand, then the orders placed with the producer, and the producer employs people?

Mr. **Brown**. Yes.

Mr. **Crawford**. Is that the situation?

Mr. **Brown**. Yes.

Mr. **Crawford**. Now, do you think that our banking system today necessarily must function in a manner that the man who sits at the bank desk must think first of his ability to be liquid when a depositor calls for his money? He is forced into that at the present time?

Mr. **Brown**. Yes, sir, he is; that is one thing he has to do.

Mr. **Crawford**. And you also feel that many people, a good many families, individuals and families have both savings accounts and small demand checking accounts, who are living far below the standard of life they would really like to live and enjoy today?

Mr. **Brown**. Yes.

Mr. **Transue**. This question has occurred to me: When this discount is put on would that raise the price of goods sold at retail to the ultimate consumer? In other words, a hundred dollar article now sells for $100. If a man goes in and the price stays the same he can buy it under the provisions of this bill at $85?

Mr. **Brown**. Yes.

Mr. **Transue**. That is, for $85 with the 15 percent discount?

Mr. **Brown**. Yes.

Mr. **Transue**. When it was on for a little while, would that $85 go up to $100 due to the discount?

Mr. **Brown**. I do not think there would be that tendency at all, because the retailer is interested in a volume of transactions, provided that his cost is covered with a reasonable profit.

Mr. **Transue**. But he can reduce profit on a certain percentage above what it cost.

Mr. **Brown**. Yes; and the 15 percent, really is reducing his costs. What is done in this case ultimately is reduce the price to include only the costs of current production.

Mr. **Transue**. You do not think it would have a tendency to put more money in circulation, the purchasing power of which would buy less in actual goods?

Mr. **Brown**. No, sir.

Mr. **Transue**. Of course, the price does go up on goods when business is good anyway, does it not, like in war times? Your money did not buy as much then?

Mr. **Brown**. Yes; that is true, but you will notice that ultimately this bill contemplates that there shall not be an arbitrary figure of 15 percent, but a discount that is based upon the difference between the capacity of production and actual production. Therefore there would really be no reason for prices to rise, no incentive to raise them.

Mr. **Transue**. That is all.

Mr. **Goldsborough**. The committee will adjourn until half past 10 Wednesday morning. Mr. Brown, on behalf of the committee I want to express our very sincere thanks for this very illuminating and interesting and thoughtful discussion that you have given us this morning.

(Thereupon, at 12:35 p. m., the committee adjourned until Wednesday, March 2, 1938, at 10:30 a. m.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

MONDAY, MARCH 7, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The Committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members present: Messrs. Goldsborough, Reilly, Williams, Farley, Ford, Brown, Patman, McKeough, Transue, Gifford, Luce, Crawford.

The Chairman. Mr. Goldsborough, the committee has met this morning to hear you resume your statement in reference to your bill, and we will be very glad to hear you.

You may proceed.

Mr. Goldsborough. Mr. Chairman, Senator Owen has a statement he would like to make before I begin, if you please.

The Chairman. We will be glad to hear you, Senator.

Mr. Owen. Mr. Chairman, it is not a statement; I rise merely to request permission to insert several tables giving some facts pertaining to the previous statement I have made, and I would also like permission to insert some explanatory matter in my statement.

The Chairman. That is perfectly all right, Senator.

Mr. Owen. I thank you, Mr. Chairman, for that permission.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. Goldsborough. Mr. Chairman, it was agreed that I should proceed this morning with a discussion of H. R. 7188, that no other witnesses should be heard on H. R. 7188 except myself.

I have no desire to depart from the terms of the agreement. It is perfectly evident that we must have orderly procedure in order to make progress.

I think, however, that it is not out of order, or beyond the terms of the agreement, for me to say that during last week I received two very interesting statements on H. R. 7188, one by Elliott Taylor, president of Housing, Inc., with offices in New York and San Francisco, and another from Allan T. Gwathmey, a professor at the University of Virginia.

Both of these gentlemen offered to appear before the committee, but I wrote and told them of the agreement, and said that, without objection, I would incorporate their statements in the record.

The Chairman. I am sure there is no objection to that.

Mr. Goldsborough. Mr. Chairman, both of these statements are interesting, but it seems to me that the very practical and immediately pertinent statement of Mr. Taylor should be transmitted to the committee immediately, and without objection, I would like to read it as a part of my testimony.

This is the statement made by Mr. Elliott Taylor.

Mr. McKeough. What is the firm, Housing, Inc.?

Mr. Goldsborough. I have a letter from Mr. Taylor, the letterhead of which carries the name "Housing, Inc." That is all I know about it.

Mr. McKeough. It is a magazine published in reference to housing?

Mr. Goldsborough. I think probably it is. It says "Housing. The magazine of low-cost homes."

I will read Mr. Taylor's statement. It says:

STATEMENT OF ELLIOTT TAYLOR, PRESIDENT, HOUSING, INC., NEW YORK, N. Y.

Reduced to its simplest terms, the true purpose of an economic system is two fold: (1) to bring into existence the largest possible quantity of consumable goods, and (2) to transfer those goods out of the production or industrial system into the hands of private individuals as rapidly and as efficiently as possible.

Any production that does not eventually and in the delivery to consumers of wanted goods and services would naturally be a meaningless waste of time and energy.

There are, of course, certain moral, social, and religious aspects of contemporary society that are also vital to human happiness. But I feel that we may seriously cloud the issue if we allow ourselves to confuse those aspects with the economic problem. The manner in which we can produce and consume to full capacity is a problem of economies. The proportionate disposition of this production to the citizens of the country is a social problem. There are those who go even further and manage to make a moral and religious issue out of such a question. Quite often in the course of a discussion they succeed in throwing off a considerable amount of self-engendered heat, but I seriously doubt that they throw any very penetrating light on the economic aspects under consideration.

We are all quite safe in assuming that our fellow citizens in general could and would consume a great many more things if they had the money to buy them, and they also would produce a great many more things if anyone had the money to pay them. If the producers are willing and able to produce, and the consumers ready and anxious to consume, doesn't it seem reasonable that we should examine the one vital link that connects the two processes—the money system? And if it can be demonstrated, as I believe it has been demonstrated, that there is a technical flaw in the financial system that, in a modern power economy, makes it forever impossible for the consumers to buy back all of the goods that they produce, would not it seem that the most realistic approach to the solution of our economic dilemma would be to find and eliminate that flaw?

The strictly material necessities of life are broadly classed under the heading of three indispensables—food, clothing, and shelter.

Since the shelter problem is the one that is most prominent in the public eye at the moment, and since shelter, or housing in its present almost hopeless dilemma best dramatizes the flaw in the system to which I have reference, let us consider certain aspects of that vexing problem and their relationship to the measures of financial reorganization Mr. Goldsborough here proposes.

I have felt that this statement would be especially interesting in view of the very interesting hearings we had in the last session of this Congress and in the present session on the question of housing (continuing reading]:

No doubt members of this committee have had many housing statistics hurled at them during the discussion of the Wagner-Steagall bill last summer and fall, and the National Housing Act amendments of 1938.

They were told, I presume, that in the years from 1923 to 1930 we built on an average of 447,000 family dwelling units a year, that during the years 1930 to 1937 we built only 74,000 such units per year. But were you ever informed that during the period from 1920 to 1937, a period that was approximately half boom and half depression times, 47.3 percent——

That is nearly one-half [continuing reading].

of all homes built went through mortgage foreclosure? Congress with the best intentions in the world has recently liberalized the terms of the Federal Housing Act, in the hope that it would stimulate a real and lasting revival of the homebuilding business of the Nation. But even if we are able to get the lagging boom in building under way, will it be any permanent solution of our housing problem if a few years of building prosperity are to be matched by an equal number of years of panic, and mortgage foreclosure on nearly half of the new homes built?

You know, of course, that there is no agency in the United States, either public or private, that actually knows how many homes there are in the country, or how many were built last year, or any year.

But there are innumerable estimates of the existing housing facilities, and estimates of the need for new dwelling units. The estimates of shortage range widely from 16,297,000 needed in the next 13 years, according to the congressional Committee on Education and Labor, down to the more modest guess of the Chamber of Commerce of the United States, that 7,600,000 new homes will be required in the next 10 years.

These requirements are not that our people may dwell in marble palaces, but merely that we maintain the standards of shelter that existed prior to 1929.

We seem to have a tendency to look back at some year—1926 or 1929—and view it in restrospect wearing a halo of social and economic perfection.

Let us suppose that, through the impetus of the revised Federal Housing Act we are able to reincarnate in the field of residential construction the year 1929. Where will we be? We will be back in a year in which we built 400,000 dwelling units at a cost of $2,623,000,000. This will be a year in which approximately 3,000,000 men were employed in the construction industry. Yet we will also be in a year in which 51 percent of our families had incomes of less than $2,000 a year, and 21 percent had incomes of less than $1,000 a pear.

This means that over 6,000,000 families were unable to pay over $10 a month rent or rent equivalent—which means of course buying a home on terms like rent—the 20-year plan of the Federal Housing Administration.

Early in 1936 Mr. Charles E. Pyndon, then of the Public Works Administration Housing Division, said: "We have not been able to consider in our plans housing for this class, which must be on a permanent relief basis. If we are going to house them we shall be obliged to reverse our conception of a financial policy. We shall have to hypothesize 100-percent subsidy at the outset, and collect whatever rents may be possible."

There in a simple and understandable statement is a recognition of the results of a chronic insufficiency in purchasing power as applied to one of the three absolute necessities of human existence. A certain percentage of our population, and apparently in our greatest year of prosperity it was about one-fifth of the total number of our families, were unable to shelter themselves within the meager reference of minimum standards of health, comfort and decency.

The Wagner-Steagall bill passed last year recognized, and formally accepted as a principle, the fact that for a portion of our population some form of permanent subsidy is a prerequisite to adequate shelter. Yet as commendable as the act was in its purpose, I believe its inadequacy within the frame-work of present financial conception is well known, and was a matter of bitter disappointment to its authors. Mr. Nathan Strauss who has been appointed to act as administrator of the United States Housing Authority foresees the construction of only 40,000 units per year, which he estimates will take care of but 10 percent of the national needs.

You know, of course, that only 25 States have legislation in a satisfactory form to enable them to cooperate in the purposes of the act; that only 50 cities have Housing Authorities; and that not all of those 50 are financially able to make the required contributions toward local projects necessary before they can obtain Federal grants.

Giving the Wagner-Steagall bill the full credit that is due its authors and the Congress in facing realistically the cold facts of inadequate purchasing power for a certain portion of our population, we must conclude that it can at the best be considered only a start in the direction of delivering to our citizens the shelter that they require, that the Nation is amply able to provide, but which they cannot pay for.

The great frontal attack on the building doldrums, however, is to be made during 1938 and the next 10 years, on the strength of the newly amended Federal Housing Act. This piece of legislation presupposes that purchasers by the millions will be able to buy, or rent, on terms that will make landlordism a profitable occupation for the great majority of the houses that are to be built.

Some of the predictions of the scope and volume of this new activity have had a note of gaudy optimism about them that does not seem to be supported by the ascertainable facts.

For example, the papers were full of reports that the administration anticipates the new market will absorb about 800,000 homes a year at an average cost of $4,000 each. It is almost universally accepted that a home buyer cannot obligate himself to purchase a house that costs him more than 20 percent of his monthly wages or salary. Following the general rule that 1 percent of the value of the house equals the monthly rental, this means that these 800,000 homes per year must be rented or bought by families with incomes of between $2,000 and $2,500 per year.

In a recent survey completed by the National Housing Committee, one of the most painstaking and complete surveys of the housing market ever undertaken, we find that there is literally no shortage of adequate homes for those who are in the income groups able to pay over $30 a month rent, while there is a shortage of 2,036,558 units for those able to pay less than $30 a month.

If this is the case, would it not appear that either purchasing power must be raised, or the cost of the home substantially lowered before we can have any hope of achieving the 800,000 units per year that have been optimistically envisioned?

This fact has been recognized, but unfortunately far too much stress has been placed on lowering the cost of building construction, rather than on increasing over a wide range the general purchasing power of those who are normally expected to buy its product. There is current a very pronounced tendency to urge reductions in wage scales on the part of the building trades employees. But I question whether those who ask the building trade mechanics to gamble their present hourly wage against hypothetical increases in annual wages have looked at the figures realistically. Our 1937 building volume, on residential and nonresidential work totaled $2,341,000,000.

Thirty-five percent of the average cost of construction is for labor on the job, which would mean that the building-trades workers drew in wages about $819,333,000 during the year. But during that year we had approximately 800,000 members in the building-trades department of the American Federation of Labor. So if those mechanics had worked exclusively at their trade during the year they would have averaged only $1,025 per year per man. But worse than that, the American Federation of Labor estimates that the building trades were only about 60 percent organized, which would mean that a total of 1,333,000 must normally have looked for their living to this 2⅓ billion in construction. If this is the case the average annual wage drops from $1,025 per man to $615.

The workingman has to be a gambler whether he likes it or not. But is it reasonable to assume that he will gamble any part of the hourly scale that netted him only $615 a year against a mythical boom in which 800,000 homes a year are going to be built for a market which, at our present level of national income simply does not exist?

I imagine it is currently supposed that in general all of the workers engaged in turning out products—whether they be vice presidents in charge of something or other, or mechanics in the shop or field—should be able to buy the products that are created or manufactured, with the wages, salaries, and dividends that they earn in the process. The shelter that the building trades employees could have bought under these conditions would be the type of shelter that they could get for an average of $10.25 per month. Or had they decided that they would like to buy, they would have been able to afford a house that cost them just $1,230.

Does not the patent absurdity of our present financial system begin to shine through, at least as far as one of the three indispensibles of life are concerned—shelter? It might be argued that every employee in the Cadillac plant should not expect to be able to buy a Cadillac, and certainly every carpenter who works on a $100,000 mansion could not be classed as a prospective purchaser of such a dwelling. But I submit it as a matter of common sense that the man who has the training and the skill necessary to do almost any job on a house that is built well enough to outlast the mortgage, rates a little better shelter than $10.25 a month would provide for him and his family.

And if it is true in all industry, as it is true in the building industry, that those who create the goods—the real wealth of the country, are never able to buy them back—who under the sun can buy them?

If it is true here, it must be true in respect to other types of consumer goods, that either the price must be lowered or incomes must be raised or the things made for sale cannot be bought.

Out of Washington in the past few years have come two rather bewildering and conflicting pronouncements. First that prices had to be raised, to restore the incomes of the producers, on the theory that additional purchasing power generated would enable more of the people to pay those prices. Just recently it was announced that prices had to be lowered so that goods and services offered for sale could be brought within the reach of the purchasing power that did not seem to get up there fast enough. The latest pronouncement seems a repudiation in part of the latter policy and a return to the former.

It is becoming increasingly obvious that tampering with prices alone will not solve the dilemma of a recession superimposed over a depression. If high prices were enough, why did 1929 culminate with black October? If low prices contained the answer, what more could be asked than the return of 1933?

The New York World Telegram in bemused speculation last week said "Perhaps what he (the President) means is that producers should get higher prices for raw materials and consumers should pay lower prices for finished goods, and maybe that could be arranged, although at the moment we do not quite see how."

Yet as a matter of fact, this very thing can be accomplished by the application of the principles behind H. R. 7188. At least, what producers would get, and what the consumers would pay would be dictated by the old law of supply and demand, instead of by the fluctuations of the purely intermediary medium of exchange—the money system.

The question really need not be as complex as financial minds would attempt to make it. After all, the only things that we produce are goods and services, and the only things that we consume are goods and services. If we want to exchange them by means of coupons or receipts, instead of bartering in kind, what is more reasonable than that there would be an adequate supply of coupons? A theater that played every night to a half empty house, or a railroad company that turned away passengers on the grounds that it did not have enough tickets would be the laughing stock of morons. Do we deserve any higher regard when we attempt to gear our national production down to fit the inadequate purchasing power of our national consumption?

Mr. Goldsborough has estimated that his bill, if it became a national policy, would increase our national income to about 100 billion dollars a year, in 18 months And there would be an immediate increase through the retail price discount of from 10 to 15 billion dollars.

I like to think of this sum in terms of the solution of our moribund building industry.

This additional purchasing power can be easily translated into terms of consumer goods, because it would go directly to consumers. It would be pumped into the system at the bottom where it is needed, and not at the top where through some involved system of cogs and flywheels it would be hoped that it would trickle down to the consumer.

Ten billion dollars increased purchasing power—allowing only the normal 20 percent of this to go for shelter and we would have in sight—in hand as a matter of fact—the money to spend $2,000,000,000 annually on new and adequate housing. Even on present buying terms that would be sufficient money to justify $20,000,000,000 worth of new homes. Not 800,000 but 5,000,000 new $4,000 homes could be constructed, or at least could be bought as fast as our physical plant and manpower were able to construct them.

Those who talk so glibly of the psychological factors of recovery—who parrot such phrases as confidence, and uncertainty, and Government interference with business might look to the building boom that never got started—the pitiful little revival of 1936 and 1937. About all the buying public had then was confidence—confidence and optimism, especially in regard to the real-estate market.

But confidence and all of the other psychological incantations that were recited did not prove quite enough. There was still a grave shortage of purchasing power, and when the building industry finally finished, taking care of the most pressing wants of those who could afford high-priced houses, the whole thing collapsed. And the reason it collapsed was because those who were supposed to buy the new dwellings simply could not afford them.

Fifty dollars a month will buy, on the average under Federal Housing Administration insured-mortgage terms, a $5,000 house. But $25 a month plus all the confidence in the world will buy only a $2,500 house.

I believe the entire building industry is ready and anxious to do its part to revive residential construction. It is keenly aware that prices must be kept down, and in many instances substantially lowered. I believe labor will cooperate, in spite of present coolness to proposals to reduce hourly wages, when it sees some tangible evidence that there is something to cooperate for.

But I believe also that both industry and labor, regardless of their determination can never win, if they are to pit their strength against a system that looks only to the restoration of pre-1939 conditions, with their post-1929 consequences.

The Federal Housing Act as amended will bring adequate housing within the reach of thousands who could never afford adequate housing before. If the benefits of this act can be augmented by an increase in purchasing power such as Mr. Goldsborough envisions, adequate housing will be within the reach, not of thousands or hundred of thousands, but of millions of American families who have long since abandoned hope of decent shelter.

Mr. Chairman, the statement of Professor Gwathmey, to which I have referred is as follows:

STATEMENT OF PROF. ALLAN T. GWATHMEY, UNIVERSITY OF VIRGINIA, ON H. R. 7188

The subject of the modernization of the financial system is unquestionably the most important problem before the world today. On the solution of this problem depends the success or failure of the scientific age; for without a satisfactory system of exchange the many advantages made possible by applied sicence, with its division of labor, become a hopeless tangle of special interests. Most of the economic evils of our day may be traced to the inability of the financial system to reflect the great wealth made possible by the modern methods of production. The application of scientific knowledge has now made it possible to banish poverty and insecurity from the world forever, but in the midst of the greatest physical wealth ever known the world stands on the verge of a financial collapse which is entirely unnecessary and which may have far-reaching consequences. Finance must be removed from the role of an uncontrollable black-magic. In no uncertain terms, finance must be made to reflect the great physical wealth made possible in our land; it fails miserably to do this today.

As a background for the discussion of why the bill under consideration provides for the necessary modification of the financial system, I wish to review briefly what might be called the high points in the development of our systems of production and finance.

Prior to the nineteenth century, the only source of power in the world, with the exception of small amounts of wind and water, was the muscle of man and beast. With the partial perfection of the steam engine by Watt in the early part of the last century, there was introduced into the then physically tired world a source of power which was destined to shift gradually the work of the world from the shoulders of a man to the tireless shoulders of a machine. With the perfection of the steam engine, the world first began to get something for nothing in a big way. Then not more than 50 years ago, there followed the development of another source of power, the internal combustion engine, together with the development of that amazing medium for transferring power, electricity. Add to these, many materials such as metals, glass, and an ever increasing number of synthetic chemicals, and we have today a system of production composed largely of automatic power-machinery which can feel, hear, and see.

A trip through a modern chemical plant is a real educational experience. The first thing which would impress the visitor would be the fact that he must look about to find a worker, and the chances are that when he did find one, the worker would be a very young man, selected for his quickness and adaptability, whose sole job was to read meters and make an occasional adjustment on a dial. From this plant would pour tons of synthetic chemicals which would be quite meaningless to the average citizen until they were converted into such useful products as textiles, fertilizers, and automobiles which we all want. It would probably also be true that due to lack of orders this plant would be running at about half of its capacity. As an example of the most modern type of power-machinery, a piece of textile equipment has been recently developed in Japan which can take one look at a piece of cloth and automatically reproduce the complicated design of the cloth. In general, it is fair to say that the modern system of production has been developed rationally with the end in view of producing the best article with the least expenditure of energy and materials. It is now a commonplace to say that the productive problems of the world have been relatively solved for the first time. Our productive system, given the orders, can furnish in almost limitless quantities and at a low cost any of the materials which are required for a satisfactory standard of living today.

But, has our system of finance been developed on a rational basis in order to serve as a convenience in the production of goods? Prior to the seventeenth century, the government in the name of the crown coined all of the money which anyone was allowed to use. Around 1650, the goldsmiths in England, finding that only a fraction of the gold which had been deposited with them for safekeeping was ever withdrawn, hit upon the epoch-making idea of issuing two receipt slips against one piece of gold. One slip went to the owner of the gold and the other went to anyone who found it necessary to borrow money in a hurry but who didn't ask questions. These receipt slips, as everyone knows, are the forerunner of the modern bank note. In 1694 the Bank of England was formed by a group of merchants in London who agreed to lend to the Government a little over a million pounds in return for the right to issue Bank of England notes up to the full amount of the loan. Not only was the Bank of England in effect to lend its money and to keep it too, but it was to obtain a practical monopoly over the creation of bank notes in the vicinity of London and ultimately in England. With the formation of the Bank of England in 1694, a private bank first began to get something for nothing in a big way. With it also came the invention of the standing national debt, which has slowly increased in importance until it ranks in the world today as unsolved economic problem number one. I wish to quote concerning the formation of the Bank of England from the distinguished English authority on banking, D. H. McLeod. "Not to a certain extent, this plan might be attended with no evil circumstances, but it is perfectly clear that its principle is utterly vicious. There is nothing so wild or absurd as this in John Law's theory of money. If for every debt the Government incurs, an equal amount of money is created, why here we have the philosopher's stone at once. Stated in simple language, it is this: That the way to create money is the way to borrow money. That is to say, A lends B money on mortgage, and on the security of the mortgage, A is allowed to create an equal amount of money to what extent he has already lent. As a general principle what can be more palpably absurd? The ravings of Chamberlayne himself, are no more wild." (Chamberlayne was the author of the land bank which failed.) It should be emphasized that this is the important principle involved in the operation of the Bank of England from which we have inherited the important features of our present financial system. Two other facts concerning the formation of the Bank of England should be mentioned. One, the formation of the bank was not accepted as a rational plan designed for the long-time good of the nation. At the time, the government of William III, of Orange, was in financial difficulties, and it either had to accept the proposal or to get out. The Earl of Mulgrave maintained that the bill to establish the bank must be passed without alteration, not because the arguments against the bank were not good ones, but because the immediate difficulties which would follow from a refusal were greater than those which would follow from its acceptance. The second point is that the goldsmiths set up a howl when the bank took from them the right of issuing an important medium of exchange.

From 1694 down to the early 1800's, the Bank of England retained a practical monopoly over the creation of the Nation's medium of exchange. By the end of the eighteenth century, the tremendous increase in productive facilities, made possible by the invention of the steam engine and power machinery, demanded an unprecedented increase in the supply of money. But this was largely prevented by the Bank of England which, while insisting on its monopoly of the right to issue bank notes and preventing the formation of the banks of issue with more than six partners, made no attempt to establish branch banks in the provinces. A method of circumventing this monopoly of the Bank of England was soon found. Following the practice used by the Dutch of settling transactions through the use of the check, new banks began to form in England which lent bank credit against a small amount of gold or Bank or England notes held in reserve. In 1833, the joint-stock banks with the right to issue bank credit were legalized in England. The Bank of England, in turn, set up a howl and fought bitterly the use of bank credit by the joint-stock banks, but finally when it was unable to stop the joint-stock banks, it shifted over about 1860 to its present position of a central bank which controls directly or indirectly the amount of bank credit for the greater part of the British Commonwealth.

As regards our own system of banking, Alexander Hamilton, trained as a boy in the West Indies in the English system of banking, simply superimposed on the United States, over the objection of Mr. Jefferson, a system similar to that of the Bank of England. Furthermore, the privilege conferred on the national banks in the United States in 1864 of creating bank notes up to 90 percent of the value of the loan to the Government was simply a scheme to sell Government bonds and had no rational basis form the standpoint of the long-time good of the country. The Federal Reserve System served to coordinate and control the banking system but in no way changed the fundamental principles under which the financial system had to operate. The important principle of the present system whereby banks possess the right to create new money and lend it to the Government or to individuals as a debt has come down to us from the formation of the Bank of England in 1694.

The following conclusions about our financial system can now be drawn:

1. The important changes in the evolution of our financial system, with the possible exception of the establishment of the central banking system such as the Federal Reserve System, have had little or no rational significance, but have taken place in times of national stress largely as schemes by which special interests received special privileges. In other words, the conventions of our system of finance have had no sacred origin, as we are often asked to believe, which would prevent modifications or changes from being made whenever conditions warrant them.

2. There has been very little direct or conscious relationship between the systems of production and finance. The modern system of production is based on the application of science which involves a continual process of change and improvement. Orthodox finance, on the other hand, seems to resist most every form of change and has failed to keep in step with the new methods of production. New industrial inventions must be accompanied by new financial conventions if finance is to reflect the ever-increasing amount of physical wealth.

3. Our economic system today generates actual costs, which must be recovered in prices, at a faster rate than purchasing power is distributed. This condition cannot be remedied by the producer simply raising wages as he is asked to do, for the increase in wages means an increase in prices which in turn neutralizes the increase in wages. Furthermore, the increase in wages cannot be taken from profits for the profits on the average are of insufficient amount to account for the shortage. The reasons for the gap between prices and purchasing power are inherent in the conventions under which our financial system must operate, and can only be considered very briefly. In general, it may be said that this gap is produced by the fact that there are a number of costs which must enter into the price value of manufactured articles which are not covered by the distribution of a corresponding amount of purchasing power. Such uncovered elements of cost are produced by (*a*) the allocation of charges for reserves, surplus, and undivided profits, (*b*) the reinvestment of wages, salaries, and dividends in the production of new goods which results in two units of price being created with only one unit of purchasing power available for the purchase of these goods, (*c*) the premature cancelation of purchasing power before the liquidation of the costs created by the distribution of that purchasing power. This last factor may not be effective in contributing to the shortage during a period of constant economic activity, but becomes of great importance when economic activity is curtailed even to a slight extent. It should be mentioned that the shortage produced by the above factors may be temporarily made up by the export of goods and the expansion in the production of capital goods.

The bill which has been introduced by Mr. Goldsborough is designed to compensate for this shortage of purchasing power. The bill is unique in the fact that for the first time the financial system is periodically and directly related to the amount of physical wealth in the country. It brings together the bookkeeping financier and the producing engineer. Specifically, it does this by first providing for a periodic estimate of the capacity of the Nation to produce goods and services plus an estimate of the actual consumption of those goods and services. Certainly there is no possible way by which finance can reflect the production of goods and services unless the Nation draws up regularly an approximate statement of the amount of this production. This is of fundamental importance. A periodic statement of wealth is the first requirement of good business, of engineering efficiency, of the scientific method. In fact it is just plain horse sense and it is difficult to see how anyone, orthodox or unorthodox, can fail to approve of this measure. It would place the financial system on a more realistic and conservative basis than the one under which it operates today.

These figures are not as difficult to obtain as they might first appear. In fact, there are several comprehensive surveys of our productive capacity in existence to-day. Every modern factory knows to a reasonable degree its productive capacity and the amount of materials consumed in operation. There may be some difficulty encountered in obtaining the initial figures for small shops and organizations which sell services, but the figures need only be approximate since a large factor of safety is employed in the use of these figures. Furthermore, it is impossible under the terms of this bill for any one organization to benefit by overstating its capacity.

The second important feature of this bill is that it raises the purchasing power of the consumer up to the limit of the national capacity to produce. It does this by creating debt-free credit money and issuing it direct to the consumer, not in an unlimited amount, but in an amount just sufficient to raise consumption up to the level of productive capacity. At this point, a reply may be made to the frequently offered statement of the banker that it isn't more money which we need, since there is plenty of money in the banks, but that what we need is more confidence, less governmental interference, and so on. The direct answer to this is that we don't need his kind of money just now, which is money that goes out to the community as a loan with a debt attached to it. And why don't we need this kind of money? The consumer can't increase his effective purchasing power by going deeper into debt to the banks. The producer can't afford to expand his production by borrowing from the banks when he is unable to sell at a profit the goods which he has already made. The Government, too, cannot continue for long to go deeper and deeper into debt to the banking system in order to bolster up the purchasing power of the consumer and thus prevent a complete break-down of trade. What the modern system of production must have, in order to survive, is a supplementary amount of debt-free credit which goes direct to the consumer in order to raise consumption up to the level of production. Then, and only then, will it be possible for the producer to borrow the money which the banks have available in order to expand production further.

It is sometimes said that there can be no such thing as debt-free money. There can be and there will be debt-free credit issued to the consumer just as soon as we decide to stop imposing on our Nation a debt-ridden system of finance. There is nothing impractical or immoral about issuing a limited amount of credit direct to the consumer. Only convention, inherited from the formation of the Bank of England, has decreed that all money must enter the economic system as a debt owed to the banking system. It simply depends on whether we wish our wealth to be reflected as a demoralizing debt or as a credit. It should be understood that as soon as the credit money issued to the consumer is spent, it circulates as any other dollar does today.

The actual injection of this new credit money into the economic system is to take place through a discount on retail sales. The discount is to equal the market price of the retail article times the ratio of the idle productive capacity of the Nation to the total productive capacity. The forces of competition will tend to control the market price just as they do today. The retailer is to be reimbursed by his bank on presentation of properly signed vouchers for having sold below the market price, and the bank in turn is to be reimbursed by the Treasury with interbank currency notes. The result of this is that the consumer gets an increased purchasing power and the producer gets an increased market. The mechanics of handling this discount are no more complicated than the system of discounts used in business or the system of dividends used in cooperative stores. It should be pointed out that this varying discount serves as an automatic regulator between finance and production just as a regulator on a steam engine relates the amount of steam to the load on the engine. It would no more tend to inflation than a regulator on a steam engine would allow the engine to run away when the loan is varied; it would keep the ratio between money and goods constant.

There are several questions which are indirectly connected with the bill and which should be touched on briefly. The first is the influence of technology on employment. Will employment increase or decrease in the future? Frankly, I don't know, and I don't believe that anyone else can tell for certain, for the answer is dependent on the rate of expansion of industry and the rate of displacing men with automatic machinery. These two factors are independent variables. It seems probable that unemployment will increase but it cannot be proved. It is not essential to settle the question just now, for there exists a large number of unemployed who must be provided for by some method. The retail discount would materially help with this problem by increasing purchasing power and by increasing employment due to an increase in production.

A question of importance is the rate at which industry can expand provided that it is furnished with a ready market for its products. I believe that industry could double its present capacity in 5 years, certainly in 10. One plant with which I was formerly associated, a highly complicated plant which fixes atmospheric nitrogen and produces a large number of synthetic chemicals, doubled its capacity without a great deal of trouble in about 3 years. It is sometimes asked, that if industry were allowed to expand continuously, would not the desires of the people for all types of goods soon become saturated? I do not think that we need worry about this being realized within the near future. The average income in the United States today is about $500 per year per person. If this income were increased each year by an amount equal to 25 percent of what it is today, it would require about 400 years to reach $50,000, an amount which is received by quite a few people who complain bitterly when their incomes are to be reduced for any reason whatever.

My discussion of this bill would not be complete without some mention of the influence of an increased purchasing power on scientific activity, that indirect force which is largely responsible for the modern age. A few cases will be cited. Dr. James Ewing, of Memorial Hospital in New York, a world authority on cancer, stated in an address a short time ago before the American Society of Cancer Control that the cure of cancer now largely depends on finding sufficient money to carry on the research. Dr. Ewing said, "Our workers in cancer research, young men with talent and enthusiasm, are forced to live a hand-to-mouth existence, not knowing one year whether they can continue their work the following. If I had a million dollars, I could find the solution to gastric cancer." In my own field, where we are attempting to study the mechanism of chemical reactions and to find out why and how two molecules react, our efficiency is reduced by at least 50 percent due to a lack of funds. It should be emphasized that both the trained workers and equipment are available, only the purchasing power is not available. The bill under consideration would go a long way toward fostering both directly and indirectly the progress of science, as well as allowing an opportunity for a greater activity in education, music, art, and many fields which would contribute to our general happiness. With the productive problems of the world taking care of themselves, so to speak, it is necessary that we prepare the way financially in order to allow a greater participation in the so-called immediately nonproductive activities of life.

The question of the future influence of science and technology on the economic system is such a highly speculative one that I prefer not to bring it prominently into this discussion. However, I wish to risk the prediction that science has just begun to place at the disposal of man knowledge about nature which would enable him to live peacefully and comfortably without squabbling with his neighbor. At present, we are suffering from maladjustment to the scientific age and from unnecessary financial difficulties. The influence of such new fields as soilless culture is staggering. I recently attended a lecture in which the method of growing crops without soil in shallow trays of water and under controlled conditions was described. It was estimated that 3,000 bushels of potatoes per acre could be grown by this method which would soon be practical. Likewise the disruption of the atom, the study of cosmic rays, the field of electronics, the study of hormones, and other subjects offer many interesting possibilities for the future. We cannot afford to allow the financial system, the bookkeeping system, to hold back such developments.

In conclusion, I wish to state in no uncertain terms that this committee and the Senate Finance Committee have the most important single job in the world today. In your hands, to a very great extent, rests the success or failure of the scientific age. Either the financial system will be brought up to date so that the people can receive the benefits of applied science in a peaceful way, or else that scientific knowledge will be used for self-destruction in one of the greatest tragedies in history. Any observant person can see that in the midst of the greatest physical wealth ever known the entire world stands on the verge of a financial collapse. The days of balancing the budget by the old conventional methods of so-called orthodox finance are over forever. We shall never get out of debt by redistributing through taxation an income which is already insufficient to purchase the goods for sale. A new financial point of view is required to meet the new methods of scientific production. There must be found a rational and peaceful solution to the paradox of an overpowering financial debt in the presence of great physical wealth. The bill which has been proposed by Mr. Goldsborough points in the right direction. It is simple in principle and it disrupts no existing institution. It strikes a balance between purchasing power and productive capacity; it provides for the use of a limited amount of debt-free consumer credit which is the next logical step in our financial evolution.

My approach to the subject and my right to appear before you may be best explained by describing briefly my own experience in the industrial world. I believe that such an experience is typical of men of my generation and will serve to illustrate a change in outlook which is taking place among technical men today. It is a change in outlook which, I believe, will have a strong indirect influence on the solution of our economic problem. I feel confident that the technical men of our scientific age will not allow much longer an out-of-date system of finance to block the efficient operation of our superb system of modern production.

As a boy, I had been convinced by men of the preceding generation that the problem of my generation was still the problem of increasing the productive wealth of this country. More factories, better farms, better transportation were needed. Particularly was this true of the section of the country in which I was raised, the Southland, which was suffering from a low standard of living. Fifteen years ago, after receiving a training in engineering, I started out with great enthusiasm on the existing job of helping to build up the industrial wealth of the Nation. It was not very long before it became apparent to me, as it has become to most every observant person, that the problem was not one of increasing the industrial wealth of the country, but was one of selling the finished products, simply one of getting orders. The state of affairs is too well known to need elaboration. On one hand was a superb factory capable of producing a large quantity of needed products; on the other was a large number of people who needed and wanted those products. In between came the financial barrier of debt and shortage of purchasing power among the consumers of the finished products. Certainly no one can deny that the problem of the world for the past 10 years has been a financial problem, one of a shortage of purchasing power. It is like having a storeroom full of supplies and not being able to get the supplies because the bookkeeper cannot work out a satisfactory system of keeping the books.

At first, it seemed that this shortage of purchasing power might be due to the exploitation of one class by another, but in spite of many such injustices, I believe that the true cause of our difficulty goes deeper than this, that the true cause is more impersonal and more hidden than the exploitation of one class by another. I firmly believe that the true cause of our difficulty, the shortage of purchasing power, is inherent in the man-made conventions under which our financial system must operate. I believe that if the angels in Heaven were to operate our present financial system, the Nation would soon end up with an over-powering debt, with factories idle, with warehouses full, and with the people inherently unable to purchase the goods for sale. The physical wealth is here to stay, and will greatly increase. How much longer will we allow a set of man-made conventions known as orthodox finance to tell us that the Nation is hopelessly in debt and and that the people as a whole cannot possibly buy the goods which are available unless they go deeper into debt to the banking system?

Mr. Chairman, I, of course, do not necessarily subscribe to all statements made by Mr. Taylor. But I do think that his statement, in its factual matter is very illuminating, and I hope will be found helpful to the committee not only in its consideration of H. R. 7188, but in its consideration of other legislation before it now, or which will come before it in the future.

The CHAIRMAN. I endorse all you have said in reference to that statement.

Mr. GOLDSBOROUGH. Mr. Chairman, the purpose of the legislation which this committee is now considering is one in which I believe very sincerely, and is the culmination of the consideration which I have been able to give the monetary problem through a period of a great many years.

I know of nothing I would not do, which is proper and decent, to see the bill enacted into law, with the exception, of course, that under no circumstances would I do anything which would embarrass the chairman of the committee. It is necessary, and as I grow older, I find it increasingly necessary, to have cooperation and orderly procedure, and to recognize duly constituted authority. But outside of the exception which I have mentioned, I feel that any energy which I can give toward furthering this legislation should be given.

I do want to say one thing, and that is this. People who make a study of a problem and devote an undue amount of time, energy and thought to it, almost inevitably lose their sense of proportion, their sense of values. They overestimate the importance of certain factors and underestimate the importance of other factors.

Now, in the consideration which led up to the drafting of this bill, every endeavor was made by me not to overemphasize, or not to overstimulate myself with any particular conception.

I have, during the entire period of my service in Congress endeavored to participate in a normal way with every activity which a Congressman should undertake. And I have endeavored not to consider the monetary problem to a point where it interfered with my usual duties, or to a point where it would interfere with my judgment. So that in whatever I have said and whatever I may say, however enthusiastically I may speak, I would like the committee to understand that I know perfectly well I may be entirely wrong, and that I honestly and sincerely would prefer the judgement of a majority of this committee to my own judgment. I mean, if and when the time comes that this or any other measure I am interested in is voted upon and the majority of this committee's judgment should be contrary to mine, I would prefer their judgment to mine because I believe it is better.

I do not know that what I have said is necessary, or even proper, but I do know that I would like the committee to feel I am approaching this matter in a practical way,

Mr. Chairman, there are a great many interesting questions which have been developed in the consideration of this bill. It is a little difficult to take them up in a purely mechanical way, but insofar as possible I am going to try to discuss some of the issues involved.

Very naturally there have been, I think, misunderstandings that have arisen as to the scope of the bill and what it proposes; and also to the administrative technique which is necessary in carrying out the terms of the proposed legislation.

A great deal of our time has been spent in the consideration of the administration of the bill. If the committee has the bill before it, I will refer them to page 3, subsection (e).

> The term "services" means passenger transportation, distribution to homes of gas and electricity for domestic purposes, rental of homes, hospitalization, schools, and theaters.

Now, the committee will remember that on the question of administration there were a great many statements made by some of the members of the committee in the matter of the impossibility of enforcing small details and—and I say this without the slightest criticism—considerable time was taken up with a discussion of how hard it would be to collect from a bootblack the discount which he was entitled to; and how difficult it would be to enforce on the part of the bootblack the allowance of a discount to the man whose shoes he shines.

Of course, there could have been only two reasons for a question of that kind. One would be that the member of the committee asking the question had not read section (e); and the other reason would be that the member was endeavoring in lawyer fashion to destroy the dignity of the conception.

Of course, there are no services spoken of here except basic services. Railroads—that is, transportation; gas or electricity for domestic purposes; rental of homes; hospitalization; schools and theaters.

Those are basic services. No minor services are included in section (e) for two reasons.

The first reason is because of the impracticability of including very minor services. And the second reason would be the fact that these minor services would be compensated for by the increased incomes of those who would receive the goods and services contemplated in sections (d) and (e).

If the income of the public in general is augmented by this retail discount in goods and services—that is, goods in general and basic services—the income of the bootblack would be augmented by the fact that his customers would be better able to patronize him and that would be the point at which he would receive the benefit of the act.

Other serious questions were asked in relation to the goods which would be furnished under the bill and the extreme difficulty of accurately determining whether or not fraud would be involved in the application of the bill, if it became law.

Personally, I never had any difficulty about administration, but in view of the questions which were asked, I have discussed, in the last few days, the matter of the administration of an act of this kind with the manager of a large department store and with those who are in charge of the international mail service. Those in charge of the international mail service state that what they actually do about all package mail that goes into international exchange is this: They first told me that for many years they had a tremendous amount of difficulty in trying to adjust the cost of these services between the various countries, but that they later adopted a system of taking an accurate count of the international mail transportation for 28 days every 3 years and the ratio which applied for those 28 days was applied for the year previous, the year in which the estimate was taken, and the succeeding year. In that way they were able, with very little difficulty, and I think practically absolute accuracy, to adjust the cost of transportation, mail transportation, between some 80 countries.

In my discussion with the manager of the department store, he stated that as compared with the details necessary to handle in a large department store, this would be baby play, as he expressed it—mere baby play. He stated that any bank in dealing with its retail customers could tell almost immediately by the difference in the general deposits and this retail discount deposit, whether or not any chiseling was going on; and that it would be impossible to continue it for any length of time at all without detection.

Mr. McKeough. Mr. Goldsborough, do you happen to know whether or not the manager of that department store had anything to do with the State sales tax in the way of experience?

Mr. Goldsborough. No. What he said was this. He said, of course, they had an ample number of clerks, and that a $10 salesman, if he chiseled for a week for a few cents a day, they could detect it by making a comparison with previous sales in that department and sales made by other salesmen; that it was almost impossible for them to take anything at all that did not belong to them, and certainly, if they did it for some days, there would be no question about their being detected.

Mr. Crawford. Mr. Goldsborough, I think that statement would be verified by almost any highly experienced insurance adjustor or high-grade public accountant.

Mr. Goldsborough. I am sure that is right. Of course, if you can help me by elaborating on that a little, I would appreciate it, because my own personal experience is limited.

Mr. Crawford. In the absence of some very abrupt increase or decrease in business which becomes known to everybody almost instantly, a concern's activity goes along on a fairly normal line; and where the necessary ratio controls are set up, which are used very greatly now by high-grade accountants—that is by corporation accountants as well as public accountants—those operating ratios run almost so accurately that the least kind of chiseling in any way whatsoever will throw the whole line of procedure out of kilter, and anybody that has an inquisitive mind can see it. It shows up on the manager's daily statement. You cannot hide it. It is there. And that pertains to manipulations of inventories, receipts, or cost of goods purchased.

Mr. Goldsborough. Thank you very much, sir.

Now, the manager of this department store also called my attention to the fact that competition, which exists everywhere—of course, where competition does not exist the present system would not work, nor would any other, because an organization could charge what it pleased—but wherever there was competition, the competitive condition itself would force the retailer to operate his retail discount accurately, because if he did not, if he undertook to swell it in any way, if he undertook to mark up his prices in any way, his competitor who did not do that would immediately get the business.

So that he felt very definitely that any difficulty of management, any difficulty of administration, would be a point of inconsiderable weight in the carrying out of this legislation if it is adopted.

Mr. Ford. Would you permit an observation at that point?

Mr. Goldsborough. Certainly.

Mr. Ford. About a year ago, the 5-and-10-cent stores, so-called, began to shoot up their prices, running up to 15 cents and a quarter. They began to take articles that used to sell for a nickel and shove them up to a dime; and articles that sold for a dime, up to 15 cents; articles that sold for 25 cents were probably not quite as good as they had been, and there was a marked increase—I am speaking now of a specific region—in the sales of small stores that sold the same articles that the department stores and the 5-and-10-cent stores were selling.

The public sensed the rise almost immediately, and the trade returned to the little store in the neighborhood, where people did not have to go downtown, and would not unless they could buy the article cheaper. They began to patronize the little corner hardware store and the drugstore that sold these same articles. There was an immediate drop in the sales of the 5-and-10-cent stores, of those articles, and they went back to the original price. It did not last 2 months.

That was observed by a so-called consumers' council that made a study of the subject, and they found it to be true that the 10-cent store immediately went back to their normal prices. When prices were going up they had undertaken to take advantage of that small rise and tack onto different articles additional prices.

For instance, I recall that on some tin articles and some crockery that ordinarily you could get in a 10-cent store for 10 cents, they raised the price to 15 cents. The little corner store that sold the same thing had always had them at 15 cents. As soon as the people found they could get them at the same price in the little corner store they stopped going to the 5-and-10-cent store. Somebody had reported this to the consumers' council and they made an investigation of it. They found that that shift had taken place within a period of 3 months.

I think the public would take care of that phase of it. I am not worried about that, so far as the administration is concerned. I think if a group of dealers made up their mind that—unless they had a very well-organized group and had gotten together very carefully then if some of them broke out and sold at a lower price in order to get a little advantage, that it would not last very long, because some of the other men in the group would go back and the thing would settle itself.

I do not think there is a great deal of danger in that, not as much as some other features. They are entitled to their opinion, but I believe that this would correct itself.

Mr. Goldsborough. Thank you, sir.

Now, there are two other considerations it seems to me that would regulate the administration, and one of them is that the law would inevitably be a popular law with the public. And it is awfully difficult to evade a popular law. In fact, it cannot be done. You render yourself such an object of obloquy in a community, if you undertake to violate a popular law, that you just simply do not do it. It is very difficult and is different than if you are violating a law that the public is not in sympathy with and has simply been enacted because of a temporary emotional national condition. But when you violate a popular law, you put yourself on the spot. You simply do not do it, if you have good sense, aside from any question of honesty and decency.

Now, another consideration is this: Any man who is a responsible retailer would understand that if he violated this law, he would lose his license forever. That is, if the violated the law and it was proven that he had. He would lose his license forever, and that would absolutely put him out of business, because he could not, after that, compete with those who got the benefit of the discount when the discount was operating. It seems to me that that would be a tremendous deterrent.

The question has been very seriously raised in the committee that the operation of a law of this kind would be giving something for nothing and that that, in principle, was bad; and that after you ascertained that a principle is wrong, it is not necessary to go any further in your reasoning, because if a principle is wrong, it is self-destructive in its operation.

Now, it certainly is true that if a thing is wrong in principle it is condemned and it is not necessary to make a further investigation. But let us see whether there is anything wrong in the principle involved here.

The more highly a people are civilized, the more often its genius is demonstrated in the work of an individual. Genius is not altogether the result of the merit of the individual, but of the society from which it springs, and the higher the society, the higher the social organization, the more often that genius demonstrates itself.

The one that makes the demonstration should, of course, receive, to a very considerable extent, the results of whatever he has been able to do. Unfortunately, an inventor is very often not the one who receives the benefit of the invention. Nevertheless, it is just that he should. But in the last analysis the society from which he springs is entitled—and all of that society—to the benefit of what he invents. And not he and not a small group that may have had the business acumen to grab the invention and make use of it. The society which has made possible that genius is entitled ultimately to its benefits.

Here we have a condition under our present monetary and industrial system in which we concede that we are not able to consume all of the wanted goods and services that we are able to produce. We concede that, all of us—every member of this committee concedes that. All right: We all work in an endeavor to consume that part of production which is possible. Then we undertake to put in operation a law which will enable us to consume the balance of it. Is there anything immoral about that? Is there anything that smacks of getting something for nothing about that? Is it better that we should receive what we can produce rather than produce and dump it over into Europe or Asia or some other place? Which is wiser? Which is more just? To produce it for ourselves or to produce it to give it away—and it does not make any difference whether we give it away by the dumping process or whether we give it away by a process of loaning money to the foreign countries which they are to respend in this country, and which debts will never be paid? And that is what has been going on in this country for years and years and years.

Now, there is another situation to which I wish to address myself. This process has been called artificial. Of course, there is nothing in civilized society which is not artificial. You cannot have a natural process in civilized society. You have to have forms of all kinds, not only in your business relations but in your social relations. But let us compare this with some of our other processes.

We have a gold exchange standard for our dealing with foreign countries. In 1934, I think it was, we devalued gold and said that gold shall no longer be worth $20 an ounce, but shall be worth $35 an ounce. What did that mean? Now, that was done to help our export market. That was the avowed purpose of it. But that meant that when we dealt with France, for instance—and I am speaking concretely in order to make my illustration perhaps more easy to use—if a citizen of France bought anything here, he could buy for $20 what he had formerly paid $35 for. That is what it meant. It also meant that a citizen of the United States had to pay $35 for what he had formerly paid $20 for importations from France.

Mr. **Gifford**. Who did that?

Mr. **Goldsborough**. I will say that the powers which direct our destinies and which were not responsible for the conditions which made that legislation necessary.

Mr. **Gifford**. Yes; I made a very long speech on that at one time.

Mr. **Goldsborough**. Now, could anything be more artificial than that?

Mr. **Ford**. I do not agree with the conclusions; however, that we paid $35 for what was formerly $20.

Mr. **Goldsborough**. That is absolutely necessary; you cannot get around it.

Mr. **McKeough**. There were some benefits, Mr. Goldsborough.

Mr. **Goldsborough**. I am not criticizing the legislation, but I am talking about the criticism of this being artificial legislation. That is what I am talking about.

Mr. **McKeough**. I have no quarrel with that premise and the example cited, but just so that the record should show that we do not acquiesce by our silence in the accuracy of the illustration.

The **Chairman**. What you mean, Mr. Goldsborough, is that by legislative fiat they changed the value of gold. They brought about a new economic development by the artifice of legislation. Let me say that it helped my people and I was glad that it was done.

Mr. **Goldsborough**. I am not criticizing it. I am mentioning it here because there has been some talk of this being artificial legislation. That is all that I am talking about.

Mr. **Transue**. Did not that act to bring into balance the relation of debtor and creditor, into the same relation that they were when the debts were created?

Mr. **Goldsborough**. Well, Mr. Transue, as a matter of fact, if that issue is going to be raised, I would like to say that I not only voted for the legislation, but I favored the legislation and still favor it. All I was trying to show was that artificial legislation is not a new thing. That is all I was trying to show.

Mr. **Crawford**. Mr. Chairman, may I ask a serious question ehre?

The **Chairman**. Certainly.

Mr. **Crawford**. On that particular point, would you assume, based on the reports that we have noticed in the papers in the last few days, that there is a fair chance that that price may move on up to around $40 or $43 an ounce, as evidenced by the large purchase of gold now being made by foreign banking institutions, the gold being purchased in this country and set aside instead of being transferred to European countries?

Mr. **Goldsborough**. Well, I am not a prophet.

Mr. **Gifford**. If you would read the New York Times of yesterday, I think you would find it very interesting.

The **Chairman**. Let me ask you in that connection, if anybody is informed, how much of this gold are we selling?

Mr. **Ford**. There is a Treasury official in the room who should be able to answer that question.

Mr. **Glasser**. The amounts of gold that we have been selling are really very trivial in comparison with the amounts we have bought since 1934.

The CHAIRMAN. I am sure that that is the fact. Still I do not know just what amounts we have been selling of late. I have not had time to look into it. I have seen references to it. I wondered if someone could give us the figure.

Mr. GLASSER. The gold stock of the United States has been reduced only to a very small extent, as judged from the daily Treasury statement in the past 9 months. I am not sure at this moment that I can give you the figures, but I could get you the figures exactly for the last month, let us say, and the last 7 months.

Mr. CRAWFORD. Mr. Chairman, would the gentleman from the Treasury Department care to comment on this phase of it? You can go back to 1934 and run through 1938. That would be roughly 3½ years. The movement started and has continued, with a jump from $26 to $27 up to $35 an ounce. Now, if these prospective holders of gold found that during the next 3½ years the price would probably shift within a range of around $15 an ounce, would you care to comment first on how they will act and what the volume will be as compared to the $5,800,000,000 that we have purchased since 1934?

Mr. GLASSER. I am not quite clear as to the question.

Mr. FORD. You have made an observation which discounted what is now taking place by measuring the small amount of gold that is being purchased compared with the jump of from $7,013,000,000, I believe it was, to $12,800,000,000; in other words, we had $4,000,000,000 in round figures and we revalued it to $7,000,000,000 in round figures. We have gone from $7,000,000,000 to $12,800,000,000. That is roughly what we have purchased in 4 years. That came to us because of a jump in the price from $26 and $27 to $35 an ounce.

Mr. GLASSER. I do not think that is true.

Mr. CRAWFORD. I will leave my statement just as it is. We will assume a shift which has started, based on reports which have been running, let us say, for 3 weeks. Certainly those purchases have been very small as compared with what happened in 3½ and 4 years when the price jumped from $26 to $35 an ounce. I am just wondering if you would care to comment on this phase of the situation. How fast may this go if they get the idea in mind that the price is going to jump say $15 an ounce as it has done before?

Mr. GLASSER. That would depend on the capital movement primarily as one of the elements in the balance of payments. This is purely hypothetical, but if the foreigners who now have capital in this country decided to move the capital out of this country into the foreign country, if they had a safe place to leave it in a foreign country, then there would be gold exports to that extent.

Mr. CRAWFORD. That is, gold exports, if they actually took the gold. They might leave it here as they are now doing.

Mr. GLASSER. You mean earmark it here?

Mr. CRAWFORD. Yes; earmark it here. In other words this gold came in here in the form of gold to the tune of $5,800,000,000. The gold was converted into dollars and those dollars remained here. They can convert the dollars back into gold in anticipation of an increase in the price of gold and leave it here for the time being, earmarked. That is what you have reference to as to the shift of the capital movement?

Mr. GIFFORD. What is the possible shift of that gold? What is the capital investment of foreigners here?

Mr. GLASSER. It is not only foreigners' investments here, but Americans may decide to transfer their capital abroad. Of course, if we talk about possibilities, they would be very large.

Mr. GIFFORD. Well, how large?

Mr. GLASSER. If foreigners took all they have over here?

Mr. GIFFORD. Yes.

Mr. GLASSER. I believe the figure of foreign investments in the United States, short term and long term, is about $7,000,000,000.

Mr. GIFFORD. And the Federal Reserve owns how much of our gold?

Mr. GLASSER. The United States Government, under the terms of the Gold Act——

Mr. GIFFORD. The Federal Reserve holds gold certificates to what amount?

Mr. GLASSER. $9,200,000,000 or $9,300,000,000.

Mr. GIFFORD. That is a total of 16 billion.

The CHAIRMAN. Mr. Goldsborough, will you resume?

Mr. GOLDSBOROUGH. Shall we get back to the issue, Mr. Chairman? Another illustration of an artificial process is what is now being done in the sterling countries, and what England has done for many years. She has undertaken since we went off the gold standard to have a free market for gold and so manipulate it as always to get a fractional advantage on every transaction she had with every foreign country.

I attempted to do the same thing in the 1935 act and I had enough votes to carry it, but Senator Owen got into the picture and went to the Oklahoma delegation and got them away from me. So I lost, I think by some four or five votes, if I remember it, Mr. Chairman.

But it seemed to me that was a better plan than a fixed price for gold. But that was not carried in the act and it probably would have been taken out in the Senate anyhow, so we are just as well off.

Mr. Chairman, there has been a good deal of discussion in the committee as to the question of whether or not this bill, if passed, would interfere with the normal monetary processes as carried out at present by the banks. I will have to discuss that question somewhat at length, but I would just as soon go ahead now, if the committee desires.

The CHAIRMAN. As we all know, there is a very important matter before the House today, and I am sure all the members of the committee want to be on the floor. So, if it is agreeable to you, Mr. Goldsborough, I think it would be better to adjourn at this time and meet again tomorrow morning at 10:30 o'clock, when we will be glad to have you resume your statement.

Mr. GOLDSBOROUGH. That is perfectly satisfactory to me, Mr. Chairman.

The CHAIRMAN. Then the committee will adjourn now, and meet again tomorrow morning at 10:30 o'clock.

(Thereupon, the committee adjourned to meet tomorrow, Tuesday, March 8, 1938, at 10:30 a. m.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

TUESDAY, MAY 3, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members present: Messrs. Goldsborough, Reilly, Williams, Spence, Farley, Ford, Brown, Patman, McKeough, Transue, Luce, and Crawford.

The Chairman. The committee will come to order.

Mr. Godsborough, you may proceed with your statement.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND—Contd.

Mr. Goldsborough. Mr. Chairman, when we adjourned yesterday I was about to call attention to the fact that there appears to be an impression that the passage of a bill of this kind would interfere with the present normal processes of the banks and of the financial system, and of the industrial system.

In that connection, I would like to call attention to the fact that this bill, if it became a law, would only operate when it appeared that the present banking, financial, and industrial system was unable to cope with the situation.

It is expressly provided in this bill that the discounts shall only operate when production approaches consumption by less than 15 percent.

The Chairman. You mean it is so drawn as to accomplish an automatic supplementing of the regular functions of the present banking system?

Mr. Goldsborough. That is another way of expressing it, and expressing it much better than I did.

Now, this country, in my opinion, is confronted very seriously with the problems which are confronting Europe. Socialists tell us that socialism is the only process whereby the people's wealth can be properly distributed, and, of course, their process is an equal distribution.

Mr. Ford. Not so equal where they are doing it.

Mr. Goldsborough. Not so equal where they are doing it; yes.

The static conception of the Russian, Italian, and German systems is that you can only distribute what the people can produce by a process of dictatorship, which works to the standardization of the actions of the masses of the people.

The statement is made on the platform and in very elaborate works of literature that capitalism and the profit system can never result in a distribution to the people of what the people can produce, and that the reason for that is that the profit system naturally takes the means of exchange to the top.

Now, it is perfectly evident to my mind that if we are going to preserve in this country the capitalistic system, the profit system, the system of individual initiative as opposed to the initiative of the mass, dictated by some supposed superman, we have got to demonstrate that capitalism and/or the profit system has within itself the power to distribute what it can produce.

This committee listened with the greatest pleasure and profit to a discussion last week by Senator Owen, in which he spoke of the results of the operation of legislation which would require the Federal Reserve System to maintain a price level which would give the people money which would have the same purchasing power from one generation to another.

Let us assume that that proposed legislation became a law, and let us assume that the other bill which is now being discussed before this committee providing for the ownership by the Federal Government of the system of Federal Reserve banks, should become a law. If those two measures, supplementing the present rules of the Federal Reserve System, were sufficient to bring consumption up to production, then this legislation which we are now considering would never have to be used.

So that there is absolutely nothing in this bill which interferes, either with the present banking system, provided it can do the job, and as long as it can do the job, or the present Federal Reserve System, as long as it can do the job, or any other legislation which is live, and has been proposed before this committee.

Mr. FORD. Supposing we did establish a stable price level, and supposing the measure you are speaking of became law, how would that tend to give people who have no purchasing power at the present time further purchasing power?

Mr. GOLDSBOROUGH. That consideration, of course, is evidently one of the reasons why I have been taking the time of the committee for the last 5 or 6 weeks, because so far as I can see it is necessary to supplement any other legislation which has been proposed by some legislation which will feed the economic system at the bottom, when it is necessary——

Mr. FORD (interposing). Will you allow me to make another observation?

Mr. GOLDSBOROUGH. Certainly.

Mr. FORD. It is perfectly obvious that under this method all of the people could, for a time, supply the purchasing deficiency of part of the people.

Mr. GOLDSBOROUGH. Yes, sir; although it is dangerous always to answer another man's question——

Mr. FORD (interposing). How would that solve the question permanently?

Mr. GOLDSBOROUGH. That is a very interesting question, of course.

Mr. FORD. May I say further, that all of the people at the present time do something that is similar to that. In the Post Office Department, for instance, we carry magazines and newspapers for less than it costs to carry them, and the taxpayer pays the deficiency, not as great a sum, however, as this might be.

But the question is whether or not, in connection with a measure of this character, the whole of the people would be justified in attempting to supply the deficiency to that percentage of the people who canont do it, and would it solve the problem, if they did.

Mr. GOLDSBOROUGH. There are probably more answers than one to your question. But I think one answer is this, Mr. Ford.

I am having gotten up now a statement of bank deposits, broken down into different classes, from 1934 up to the end of 1937. It has not been completed yet, and for that reason I cannot bring it to the committee this morning. The Federal Deposit Insurance Corporation has it for that year.

But I am convinced, insofar as I am concerned, and I think there is no possible doubt about it, that when those figures are broken down they will show that most of the funds which have been utilized by the Federal Government to prevent extreme want among the people in the last 3 or 4 years have gotten to the top and are now in the bank deposits, not of those who originally received the benefit, but of the same element which, before the depression, had the principal amount of the riches of the country.

One of the reasons why I am having that broken down is to show the necessity, under a capitalistic and profit system of feeding society in at the bottom. That is one reason.

And the second reason is to show that while it may be true that one class of people are furnishing funds for another class, as a matter of fact, all portions of our economic society will be benefited by the passage of this legislation because when this discount is fed in at the bottom it will get to the top, and when it gets to the top it can be utilized.

So, our contention is, and I have so argued here before, that it can be utilized by those who have to pay, I will say, the income tax, and without the raising of the present rates, they will pay into the Federal Treasury over 2 billion dollars more than they are paying now, and that society, by virtue of the employment given under the operation of this act will have its expenditures for relief lessened by at least 2 billion dollars. So that, if the operation of this bill raises the income of the country to 100 billion dollars a year, the income from taxation, without raising the present rates, will be increased by over 4 billion dollars.

You have raised, I think, in your question, a collateral question, as to whether or not, assuming that what I have said already is incorrect, that all elements of society will not be benefited—assuming that is incorrect, and that the argument is not convincing, I believe one can be advanced that is convincing.

Let us assume, solely for the purposes of the discussion, that we are now producing 60 percent of the wanted goods and services which the people of this country could consume, and that that 60 percent is all that our people are able to buy, because of want of buying power.

Now, if that production could be increased to 100 percent of wanted goods and services, and assuming our present production is 60 billion dollars, that production would be increased to 100 billion dollars, the benefit of that increased production would not go ultimately to the classes of the people who get the discount; in the first instance, it would go from the consumer to the retailer, it would go from the retailer to the wholesaler, and it would go from the wholesalers to the manufacturer, and the prime producer.

The benefit of increased buying power in the hands of the masses of the people would permeate all society, and the very class, which it would appear in the first instance would have to furnish buying power, would ultimately be the greatest beneficiaries.

There may be a flaw in that argument; I do not know; but that is my argument.

Mr. **Ford**. Of course, the man who puts up the money for an enterprise in the first instance, in order to carry it for 3 or 4 years until it becomes successful, ultimately reaps the greatest benefit.

Mr. **Goldsborough**. Yes.

Mr. **Ford**. Although the original investment looked like a lot of money.

Mr. **Goldsborough**. Of course, I can understand without the slightest difficulty just how certain members of the committee feel about what is called, in the bill, interbank currency. It would have been a great deal better, possibly, to have used a different term.

Mr. **Ford**. I am a little bit in the dark on that myself.

Mr. **Goldsborough**. I am not sure but what it would have been a little better for that to have simply been called interbank credit, and I will try to explain what I mean by that statement.

If a bank, under our present system, needs cash in order to reestablish its reserve, the ordinary process is to go to the Federal Reserve bank and give the Federal Reserve bank a note, secured by collateral, in order to get the Federal Reserve notes to reestablish the bank's reserves.

But the bank does not get any notes unless there is a run on the bank. What the bank actually gets is a credit on the books of the Federal Reserve bank of whatever amount is indicated by the discount transaction. That is what happens.

Mr. **Ford**. It puts up collateral and gets credit on the books.

Mr. **Goldsborough**. It gets credit on the books. In the operation of this so-called interbank currency, all that would happen, ordinarily, would simply be a bookkeeping balance passed from bank to bank, by virtue of the operation of this interbank credit. No currency would ever pass unless the individual bank that has the credit on the books of the Federal Credit Commission actually needed cash.

Now, when we tried to round out the bill a provision was made that the interbank currency could be translated into cash, if needed.

But let us look at the present situation and see whether that condition would probably every arise.

The Federal Reserve Act now provides that a bank can take a Government bond, say, of $1,000 and attach it to a note and get credit on the books of the Federal Reserve bank of a thousand dollars, and, of course, it can get a thousand dollars in Federal Reserve notes, if it wants Federal Reserve notes.

Mr. **Williams**. There would be a pay day come, would there not?

Mr. **Goldsborough**. You will have to explain that question.

Mr. **Williams**. By that I mean a bank which borrows money from the Federal Reserve bank could not continue to get credit indefinitely, could it? Have they not established a very definite policy that they will not make these continuing loans to a bank to strengthen its reserves?

Mr. **Goldsborough**. I may not have the full purport of your question. But the law at the present time is that you can take a Federal Reserve note—and a Federal Reserve bank could not refuse—you can take your note, or the bank note——

Mr. **Williams** (interposing). I do not think you could say that the Federal Reserve bank could not refuse; I think they could refuse. I think they have refused in cases where there has been a continuous borrowing by a member bank from the Federal Reserve bank.

The idea I have is that there will be coming a pay day on the part of the member banks to the Federal Reserve bank. In other words, they cannot continue to borrow, borrow, and borrow, to straighthen their reserves. They have to provide the currency, have they not?

Mr. **Goldsborough**. No; they do not have to provide currency.

Mr. **Williams**. How much currency is there in the Federal Reserve banks?

Mr. **Goldsborough**. I cannot answer that question.

Mr. **Williams**. Do you have any idea?

Mr. **Goldsborough**. Probably you have——

Mr. **Williams** (interposing). I am asking for information.

Mr. **Goldsborough**. I do not know.

Mr. **Williams**. I was wondering what is the amount of currency in the Federal Reserve banks.

Mr. **Ford**. I do not know what the figures are, but it is what they can manage to get with the collateral, and such notes as they have, and such gold notes as they have.

Say they have $90,000,000, with 40 percent gold. Their note issue would be governed by what collateral they have from member banks, plus the gold certificates in the Treasury.

Mr. **Williams**. Of course, gold certificates, or gold from the Treasury, is another thing.

Mr. **Goldsborough**. I assume, Mr. Williams, you and I agree that this gold which is now in Kentucky is really a reserve of the commercial banks of the country.

Mr. **Williams**. Yes; while the Treasury owns it. The certificates back of it belong to the Federal Reserve banks.

Mr. **Goldsborough**. And represent cash reserves.

Mr. **Williams**. And the basis upon which they can issue notes.

Mr. **Goldsborough**. That is correct. That being so, the banks, even on the 5-percent basis, could expand to something over 100 billion dollars, based on what collateral they have, and the Government bonds that they own; they could expand that business in cash as they needed it, over 100 billion dollars, and the deposits of the country would then represent twice as much as they have ever represented before. That amount was 56 billion dollars in 1929.

Mr. **Crawford**. Did I understand you to say, Mr. Goldsborough, that the member banks could take their notes, collateralized by Government bonds, their direct obligations, to the Federal Reserve bank and secure currency?

Mr. **Goldsborough**. Yes, sir.

Mr. **Crawford**. Referring to Mr. Williams' question, if they can do that with $100,000 worth of Government bonds, as long as they can bring forth those bonds, is not the Federal Reserve bank, the Federal Reserve agent, and the Treasury, under the present law, in a position where it is mandatory on their part that they continue to supply them currency?

Mr. Goldsborough. Of course, I do not like to get into a direct difference of opinion with a member of the committee, but that is the law, as far as I understand it.

Mr. Patman. Let me make this suggestion, Mr. Goldsborough, as to the amount that could be expanded. There is approximately 13 billion dollars of gold held by the Government as a part of our currency system. If the Federal Reserve System were to issue all the money it could on that gold there would be an amount of 32 billion 500 million dollars. That would go out to the banks and they could expand on an average of 6 to 1, which means, under the present reserve requirement, that gold could be, today, based on their present system, utilized to issue 195 billion dollars.

Mr. Goldsborough. Thank you very much, Mr. Patman.

Now, I want to come, apparently leaving that point, but not actually leaving it, to a question which has been raised by members of the committee as to whether this interbank currency would not be money which is not backed in the ordinary way, that is, according to the system we now have. Let us see how we can visualize that inquiry.

If a Government bond is taken to the Federal Reserve bank by a commercial bank, a bond of $1,000, the commercial bank receives on its note, with that bond as collateral, a thousand dollars.

What does the Federal Reserve bank do? The Federal Reserve bank segregates $400 in gold as a basis to support that loan. But it leaves $600 unsupported by any other collateral except the faith and credit of the Federal Government.

So that every time the Federal Reserve bank discounts a note of a commercial bank, based on a Government bond, six-tenths of the money which it issues is fiat money, in the ordinary sense in which that term is used, because it is not supported by commercial collateral; it is only supported by the faith and credit of the Federal Government.

Of course, there are members of this committee who think that faith and credit is the proper credit upon which Government money should be based; but I mean even so far as those members of the committee who do not agree are concerned, the fact is that under the present law that is so, that money issued by the Federal Reserve bank, based upon these loans, which, in turn, are based upon faith and credit is fiat money.

So, when that statement, if it is correct, and I am sure it is, is coupled with the fact that we are on a managed currency basis now anyway, any idea that we are going out of the ordinary processes of banks in issuing this interbank currency, in my view is not justified.

Mr. Patman, and I am sure his figures are accurate, although I have not made a calculation—according to Mr. Patman's statement, our money could be expanded, without any violation of law, nearly 200 billion dollars, which would create unheard of inflation, and disastrous inflation.

As a partial restraint on the temptation to inflation, the Treasury Department, without any justification in law, so far as I know, have undertaken to take one billion 200 million dollars of gold and freeze it, and say, "This particular gold shall not be utilized at all as a basis for bank reserves."

Mr. Reilly. Did not the Treasury Department do that under authority of law?

Mr. Goldsborough. I have asked several of those in very high authority what law justified it, and they have raised their eyebrows and told me to consult the attorney for the Treasury Department. I did not do it because I was thoroughly convinced in my own mind that there was no legal justification for it. There may have been a kind of justification for it, but if there is any legal justification for it I do not know what it is, because our whole banking system is based on a gold reserve, and if that is so, you have no right to freeze any part of it, and if you can freeze that amount you can freeze all the gold in Kentucky.

Mr. REILLY. Did not the Treasury Department freeze that gold because they thought they were getting into a condition of inflation?

Mr. GOLDSBOROUGH. Yes.

Mr. REILLY. Then it is a difference of judgment.

Mr. GOLDSBOROUGH. No; what I am saying is that while they may or may not have been justified in doing it, in my opinion they had no legal right to do it, because our whole monetary system is based on the theory that our money must be backed by a gold reserve somewhere, and if that is true, then the gold in this country is sacred; it is to be used for the purpose of supporting bank reserves, and the Treasury Department, and nobody else, has any right to segregate it and take part of it away from the people. If they have a right to segregate $1,200,000,000, then they have a right to segregate every dollar in Kentucky, and cause the worst deflation the country ever saw.

Mr. PATMAN. There was another reason given by the Treasury at the time, and that was that they were apprehensive that there would be sudden withdrawals of gold, and if they permitted the gold to flow into the monetary system and there were sudden withdrawals it would cause a deflationary condition.

But the fallacy of that argument is that the Treasury has 2 billion dollars in a stabilization fund, and if there would have been any sudden withdrawals that stabilization fund would have taken care of it.

Mr. WILLIAMS. What harm was there done by sterilization of the gold?

Mr. GOLDSBOROUGH. I do not know of any. My statement was that it was done without authority of law, not that it did any harm.

Mr. WILLIAMS. How could it cause deflation when there is already——

Mr. GOLDSBOROUGH (interposing). It could not. Mr. Williams. I did not say that; I said as far as I know, the Treasury Department had no authority at law to do what it did. I do not say it would cause deflation; I did not even mean to intimate that. I think that it was morally wrong for them to do it.

As a matter of fact, with all of this gold we are on a managed currency basis, anyway. The country is not on a gold basis. A gold basis would create this tremendous inflation which has been discussed.

We have sterilized $1,200,000,000 of gold, so, as a matter of fact, money is being conducted on a managed currency basis, and as long as we continue to pay $35 an ounce for gold, and the secondary gold deposits can be mined profitably in the Rand, in the West, in Alaska, in the Klondike, of course the quantity of gold will increase. And as the quantity of gold increases we will have to go more and more on a managed currency basis, which is what we have actually been getting. And, as a matter of fact, gentlemen, no country has behind its money anything, or will have anything except a stable government and the wealth of the country.

Mr. WILLIAMS. What is managed currency, Mr. Goldsborough?

Mr. GOLDSBOROUGH. Managed currency is currency which those in control of the monetary system endeavor so to handle as to furnish the desired and proper amount of money to transact the business of the country.

Mr. WILLIAMS. We have that system now, have we not?

Mr. GOLDSBOROUGH. I think so.

Mr. WILLIAMS. Who manages it?

Mr. GOLDSBOROUGH. The Federal Reserve System is attempting to do so, as well as they can.

Mr. WILLIAMS. Do you think their powers are sufficient, under the present law?

Mr. GOLDSBOROUGH. Well, I expect their powers are sufficient, but I think probably, Mr. Williams, that the inherent difficulty is that the successful operation of that authority requires almost superhuman wisdom. It seems to me that is the major difficulty. And another difficulty is that——

Mr. WILLIAMS (interposing). If they have the proper power, if they have the authority now, under the law as it is now, then it is only a matter of administration, is it not?

Mr. GOLDSBOROUGH. I do not think so, Mr. Williams, and I will tell you why.

Mr. TRANSUE. Will you state what mechanics they should use, if they had the wisdom and judgment you are talking about?

Mr. GOLDSBOROUGH. The mechanics they would use would, of course, be the mechanics possible under a system where our money is based upon bank debt. They cannot go beyond that because of the limitation of their powers.

But the principal thing they would do within their powers would be to have what are known as open-market operations, the buying of Government bonds at a time when more money was needed in circulation, and the selling of Government bonds at a time when it appeared that inflation was about to take place.

Of course, they have other powers; they have the right to raise and lower the rediscount rates and loans made to commercial banks.

Mr. WILLIAMS. The question in my mind——

The CHAIRMAN. And regulate Reserve requirements?

Mr. GOLDSBOROUGH. They can regulate Reserve requirements under the 1935 act.

The CHAIRMAN. Which is a very far-reaching power.

Mr. GOLDSBOROUGH. If they see fit they can raise them, and then, if they see fit they can lower them again.

Mr. WILLIAMS. The question that is running through my mind in reference to all these matters is whether or not under our system the Federal Reserve Board have the power now, in fact, to manage the currency, you might say, in the interests of the people of this country, as the Board is now constituted, and if they have not that power, why not give it to them? That is why I am asking the question.

If they have not that power, what additional power should they have?

If they have it and do not administer it like they ought to do, we, of course, ought to get a different board. But if they do not have the power to do these things, if they cannot do them, then we, as a Congress, ought to give them additional power, and we ought to direct our attention to trying to find out what those things are.

Mr. GOLDSBOROUGH. Do you mind saying what you have in mind, because your question to me is not quite clear.

Of course, it is perfectly evident that the Federal Reserve System does not have any power now to create a discount on retail purchases, to ultimate consumers, and if that is a wise power, they have not got it.

Mr. WILLIAMS. Then your idea would be to give them that power?

Mr. GOLDSBOROUGH. No; and I will tell you why.

Mr. WILLIAMS. If that is a necessary thing in order to control and manage the currency of this country, why not give it to the Federal Reserve Board?

Mr. GOLDSBOROUGH. I will tell you why it was not given to the Federal Reserve Board in this bill.

This bill was deliberately framed on the theory that the present monetary and banking system of this country should be allowed to function exactly as it functions now, provided it is able to do it. It was done deliberately, as far as I am concerned, and I was months and months in deciding what was the best way in which this situation could be handled.

Mr. WILLIAMS. That would not interfere with it, would it?

Mr. GOLDSBOROUGH. If it was given to the Federal Reserve System and placed in the ordinary commercial bank system, it would entirely change the whole plan from money created by debt to money not created by debt.

Mr. WILLIAMS. They need not use it any more than the Federal Credit Commission would use it, if it was not necessary.

It would be a power to be exercised in case the powers they already have were not sufficient.

This all comes back to the question——

Mr. GOLDSBOROUGH (interposing). I fully agree with you.

Mr. WILLIAMS. If they cannot do what ought to be done, then we certainly ought to give them the power to do it.

The CHAIRMAN. Let me make an observation which I think is very pertinent.

There are many of our best counselors who hold the view, and I am fully persuaded that that view is sound, that we should not stop with the mere extension of powers and authority to the Federal Reserve Board, leaving them at sea, if they should so regard the situation, as to what the legislative intent and purpose are; but that there should be written into the law a mandate to the Federal Reserve Board, to their open markets committee, and to the Treasury of the United States, which has the powers in connection with the Federal Reserve System, that they shall use their powers for the purpose of accomplishing the legislative intent.

Mr. WILLIAMS. What would that be?

The CHAIRMAN. I am just going to undertake to say.

We passed a bill in 1932, at the first session of that Congress, when there was a change in the political complexion of the committee. I do not mean to say it was entirely due to that, but as a matter of fact, the older members of the committee will remember that the gentlemen of the present minority held the same view that some of us did.

For instance, our late dear friend, Mr. Strong, was very active about it.

Mr. GOLDSBOROUGH. And Mr. Luce supported the bill also.

The CHAIRMAN. Yes. We passed the Goldsborough bill in 1932, and in that bill we instructed the Federal Reserve Board and the Treasury of the United States to conduct their operations and use all their powers toward the restoration of the 1926 price level, and to so use their powers as to stabilize the value of money, or the price level, on that basis. Senator Owen called attention to that the other day.

I have always believed that that was a scientific bill. I would not undertake to say that that measure could not have been improved upon; I never felt at the time that it said just exactly all that I had in mind, a crude idea, unexpressed, in reference to the situation. But I have always believed it was a wise measure and that if followed up by proper administration that it would have cured many of our ills. I believe it now, although I am not of the opinion, from the advice I have had from experts and those whose judgment I trust—I am not sure that the price level alone would accomplish what we desire.

The big thing, after all, that we all desire is employment, so that everybody who wants work can get work and consume.

I believe that with the proper adjustment of the price level you would accomplish a large measure of your employment that is desired.

But I cannot say to Mr. Williams that I could write a mandate this morning that would be entirely satisfactory to myself. I recognize that conditions change, that the problem is intricate and difficult, and I have reached the age when I find myself unlearning many things that I thought I knew, about which I am mistrustful of my judgment.

But I believe that the bill we passed in 1932, if properly administered, would have brought a large measure of relief. I have said this to the committee before.

I believe if you could, in any way, bring about such a regulation of prices—I do not care; it does not shock me to say the price of money or the price of farm products, because, as I look at it, it is only a relative term—but I believe that if the farmers of this country today could be put on a solvent basis so that they could be assured of enough return for their labor, as expressed in the prices paid for the products of that labor, to enable them to consume and live according to the standards of people placed as we are by Providence, in this country—I believe if the farmers of the country were on that basis there would be such an enlargement of consumption overnight as to empty the stores of the goods on their shelves, which would in turn empty the warehouses, which would in turn create activity in the manufacturing centers and require the utilization of the idle labor of men who would be called back to work, who would themselves be going to consume, and bring about a further increase of consumption.

And I believe it is possible to do it, and if they do not—I am not sure about it in my own mind—if our financial machinery is not so equipped as to enable them to deal separately with speculative developments in the stock markets from what they must deal with what I would call legitimate trade in commerce of the United States, then that power should be enlarged.

I believe the Federal Reserve System has the power. So I would answer your question in the affirmative.

Mr. WILLIAMS. You think they have the power to raise the general price level to that of 1926 and maintain it there?

The **Chairman**. I do.

Mr. **Williams**. Of course, we have been told a number of times by the Chairman of the Federal Reserve Board that they have tried their very best and cannot do it. They claim they have not got the power and cannot do it.

So we come back to the question of the administration of the act.

The **Chairman**. I think that is where we are, and I would be less than frank if I did not say it.

Mr. **Ford**. Did we not have something in the 1935 bill for which a substitute was offered, I believe, by Mr. Glass.

Mr. **Goldsborough**. I think that is not correct. The great controversy in connection with the 1935 bill was the question as to whether or not the Federal Reserve Board should have the power to raise the reserves of the member banks. That was the fundamental controversy.

Mr. **Williams**. We had a controversy over the raising of basic commodity prices as distinguished from general wholesale prices.

Mr. **Goldsborough**. That was on an amendment offered by me, which was defeated in the House. I was talking about the time when the bill was in the committee. I think the principal discussion was on the question of whether or not the Federal Reserve Board should have the right to raise reserve requirements of member banks.

When the bill came to the committee it was provided that they should have the power to raise the reserves, in their discretion.

Mr. **Williams**. Without any limit.

Mr. **Goldsborough**. Without any limit. When this committee got through with it it gave them the right to raise reserves 300 percent, and that is the way the bill passed the House.

But the Senate bill had no provision at all for the raising of reserves by the Federal Reserve Board, and when we got into conference this was the situation.

I think at that time the Senate conferees were very much opposed to it, and I think with the exception of myself the House conferees were personally indifferent to it. That is my recollection.

Of course, they supported the position of the House, but they did not care about it personally, I think.

I raised this question with Mr. Glass and Senator Bulkley. I said this right given to the Federal Reserve Board to raise these reserve requirements tends to do what the Senate conferees claim they want to do, and that is to prevent inflation.

Finally, we came to an agreement that the Federal Reserve Board have the right to raise the requirement 100 percent.

Now, what has happened? Long before this reserve requirement was made certain members of the Federal Reserve Board kept insisting that it should be made to prevent inflation. It was resisted by other members of the Board.

It was urged by the great bankers, principally by the Chase National Bank, by Mr. Aldrich and by his economist, Dr. Anderson. You can judge as well as I can about what they had in mind.

But the fact is, in my opinion, that the Federal Reserve Board used their best judgment when they said that it should be raised, and the result has been just what some of us thought it would be, another very serious incipient depression.

Mr. WILLIAMS. In other words, you think they made a mistake in doing it, or that it was an error in their judgment?

Mr. GOLDSBOROUGH. It was an error in their judgment.

The CHAIRMAN. I thought so so strongly that I even made a statement to the press about it, something which I very seldom do.

Mr. WILLIAMS. It was done in three different installments.

The CHAIRMAN. There is a continuous, senseless clamor over this country about inflation, with millions and millions of people unemployed, and crop curtailment plans under way, and yet it is said on all sides that a third of the people of the country are living upon a standard that is a source of concern and alarm.

Mr. WILLIAMS. Let me ask you this question, Mr. Goldsborough: In view of your statement that you think it was an error of judgment on the part of the Federal Reserve Board in making the provision they did for reserves, as I understand you, you are in favor of that power, that unlimited power?

Mr. GOLDSBOROUGH. That is unlimited power.

Mr. WILLIAMS. When, in your opinion, should they exercise that right?

Mr. GOLDSBOROUGH. I am just coming to that.

Mr. WILLIAMS. I was wondering, if we had, say, 3 billion dollars in excess reserves, which I believe was the fact at that time, it was not time to put on some kind of brakes along that line. Where would you begin?

Mr. GOLDSBOROUGH. I think I can answer that in two ways, Mr. Williams.

The ordinary financial answer, I think, would be that until those reserves again had been called upon at a rate which past history showed created greater banking deposits than were safe—I will say sixty-five or seventy billion dollars—it should not have been used. I think that would be the answer I would give as a banker or financier.

But my own personal answer would be this: That inflation cannot occur until you have gotten to your people all that your people can consume of wanted goods and services, to the limit of your productive capacity, then if you keep on putting out money after that you will have a rise of prices, true inflation.

The CHAIRMAN. You have answered it perhaps better than what my answer is, but my answer, as I was going to state it, is this: It does not make any difference whether there is 1 billion dollars of reserve or 40 billion dollars of reserve; or whether there is 1 billion dollars of actual currency or 50 billion dollars of actual currency, to the citizen who wants employment, and return in the form of wages sufficient to enable him to support his family.

In other words, the true basis, and the thing upon which your eye should be fixed, is the record of general conditions, and when they are right, then stop. Then your policy is, if they go wrong, to shape your policy to get them back right again.

To look merely upon the amount required, the amount of money in circulation, does not get you anywhere.

Mr. WILLIAMS. In other words, you would wait until we get to the shape we were in in 1929 and then do it all at once?

The CHAIRMAN. No; those things do not happen overnight.

Mr. WILLIAMS. That is where you would land, in my opinion.

The CHAIRMAN. Maybe so, but that is not my view of it.

If you will remember the developments back in 1932, for quite a long time there was considerable discussion.

Senator Glass, according to my recollection—and if I am wrong I hope I will be corrected—even wrote the Board; I know he talked about it a great deal, saying that they should have turned over on their restrictive policy, to prevent the drift that occurred.

Those things do not happen overnight. I do not believe this operation can be conducted on a basis of mathematical certainty.

But I have never heard a man come before this committee and express the view that these powers can accomplish these results who, before he got through, would not wind up by telling you they can do it, but if you ever started an expansion of money that you will go on an inflated basis before you get through.

Mr. GOLDSBOROUGH. May I call your attention to a situation that existed from the year 1920 up until the collapse of 1929. Mr. Strong and I talked about it a great many times. He was endeavoring to and did it very successfully, stabilize the value of money.

But he was confronted with this situation, that industrial prices were going up when farm prices were going down. The farmers had no prosperity between 1921 and 1929.

The CHAIRMAN. Absolutely none.

Mr. GOLDSBOROUGH. The consequence was, while he was doing all he could to keep up the average, as a matter of fact, one great mass of the population was increasingly losing buying power; that is, the agricultural buying power was decreasing.

Mr. WILLIAMS. I think that is true, but what could the Federal Reserve Board do, or what could they have done to remedy that situation?

Mr. GOLDSBOROUGH. Under their present powers?

Mr. WILLIAMS. Yes.

Mr. GOLDSBOROUGH. I would not have known.

Mr. WILLIAMS. Then you get back to the question that I originally asked you, and I think there is some question in my mind whether they have the power to do those things.

It is a serious question in my mind whether they have the power we talk about under our present law to raise prices to a certain level and maintain them there. I do not believe they can do it.

Mr. GOLDSBOROUGH. They can keep up the average.

Mr. WILLIAMS. They can help.

Mr. GOLDSBOROUGH. They probably could keep up the average.

The CHAIRMAN. They can approach it.

Mr. GOLDSBOROUGH. They can approach it. It certainly was a problem.

I happen to know, because Mr. Strong was very approachable, and he would talk to you, if you wanted to talk to him.

For several years he appeared before the committee, and I called his attention to the fact that agriculture was in terrible shape, the farmer's income was not increasing but diminishing, and I did not see how in the world this thing could go along, with this loss of income, without a collapse, and that the attempt to have an average price level would not work out the problem.

I think the collapse of agriculture had as much to do with what happened in 1929 as anything else.

In 1929, in that very year when people were talking about universal prosperity, when people were talking about a change in conditions, that we were in a new era, at that time agriculture was at one of its lowest ebbs.

Mr. **Williams**. Do you believe there is anything in this policy we have been trying to carry out, regulating a certain measure of production in agricultural products to stabilize prices by following that policy we have been following as a course——

Mr. **Goldsborough** (interposing). Of course, Mr. Williams——

Mr. **Williams** (continuing). That is, to fix the farm price level within certain limits?

Mr. **Goldsborough**. I have felt that that was exactly a wrong way to approach the problem. I have felt that the legislative body had within it means and power to bring consumption up to production, rather than to reduce production. That is the way I felt about it, and the result of my feeling is this bill which we are now considering. I have never understood why it is——

Mr. **Williams** (interposing). Whether it is right or wrong in principle, does it do the job? Has it had any effect on the commodity or farm prices?

Mr. **Goldsborough**. Of course, you know it has not up to this time.

Mr. **Williams**. Did you say it has or has not?

Mr. **Goldsborough**. It has not. You mean this restriction of production?

Mr. **Williams**. Yes.

Mr. **Goldsborough**. I do not think so.

Mr. **Williams**. You did not think it has had any effect at all on farm prices?

Mr. **Goldsborough**. If it has, it is because they would have been lower than in previous years.

You will not find, for instance, that cotton was any higher than it was from 1899 to 1914, at the beginning of the war. You can take the average from 1899 to 1914, until the beginning of the World War, and you will find it was higher than since the cotton production restriction.

Mr. **Williams**. It is very much higher than in 1931, 1932, and 1933.

Mr. **Goldsborough**. Yes.

Mr. **Williams**. And the question is whether that has done it?

Mr. **Goldsborough**. Yes.

Mr. **Transue**. The competition of world markets has a great effect. Anything you can do in that direction will aid us that much. It seems to me the prices of cattle have been very materially rising because of things that have been done.

Of course, where you have a big surplus exported to the outside world you have this problem more than in any other field.

Mr. **Goldsborough**. Undoubtedly the first effect of devaluation was to increase immediately the prices of the commodities of which we have an exportable surplus. But you cannot keep up a horse trade like that.

The **Chairman**. Certainly not; we will soon have all the gold.

Mr. **Spence**. Have we mentioned duties in the exercise of power to obtain certain objectives?

Mr. **Goldsborough**. No.

Mr. SPENCE. Is not that an obligation of legislative power when we delegate that without limit or definition?

Mr. GOLDSBOROUGH. What we have already done?

Mr. SPENCE. Is not that an obligation of the delegation of legislative power?

Mr. GOLDSBOROUGH. I think so.

Mr. Williams called my attention—I do not know that anybody noticed it except Mr. Williams and myself, but he called my attention to the fact that I had advocated the giving of the entire power to raise reserves, and that I had said that they had used the power we did give them unwisely.

I did do that, and my reason for doing that, however, was that what I had in mind at that time was that it would enable us eventually to get away from this fractional reserve system.

It did not occur to me at that time that the power would be used in a way which would cause the people of the country to lose their confidence in the stability of the monetary system.

But the difficulty is this, as I see it, and this is a difficulty which I believe I have always found in legislation, that when we pass a law in Congress which is anything more than an administrative direction, which leaves discretion in one man or just a few men to do something that affects the welfare of 127,000,000 people, you are wrong every time you do it. That is the absolute conclusion I have reached.

The CHAIRMAN. There is not the slightest doubt that every citizen of this country, wherever it is possible to have it, wants government by law. That is the idea in which we believe, but we do have to trust the administration of some of the acts of Congress to administrative officers, in the complex situation in which we find ourselves today.

Mr. FORD. May I make just one observation? If it is wise to subsidize the farmer not to produce, what is wrong in subsidizing the consumer to purchase, and if you do the latter, have you not thus obviated the necessity for doing the former?

The CHAIRMAN. Since there is a very important matter for consideration in the House today, we will adjourn at this time, Mr. Goldsborough, and hear you again at 10:30 o'clock tomorrow morning.

(Thereupon the committee adjourned to meet tomorrow, Wednesday, March 9, 1938, at 10:30 a. m.)

MONETARY POLICY OF PLENTY INSTEAD OF SCARCITY

THURSDAY, MARCH 10, 1938

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee resumed hearings on H. R. 7188 at 10:55 a. m., Hon. Henry B. Steagall (chairman) presiding.

Other members of the committee present: Mr. Goldsborough, Mr. Reilly, Mr. Williams, Mr. Spence, Mr. Ford, Mr. Brown, Mr. Transue, Mr. Gifford, Mr. Luce, and Mr. Crawford.

The Chairman. Mr. Goldsborough you may proceed with your statement.

STATEMENT OF HON. T. ALAN GOLDSBOROUGH—Resumed

Mr. Goldsborough. Mr. Chairman, in the committee there has been considerable discussion about the nature of the so-called interbank currency, or interbank credit, and I have endeavored to make up a typical statement which would indicate just the effect of that currency on the bank's bookkeeping.

(The typical bank statement referred to is reproduced below:)

Typical bank statement

ASSETS		LIABILITIES	
Cash in vault	$100,000	Deposits	$10,000,000
Balance in Federal Reserve	2,400,000	Capital stock and surplus	2,000,000
Loans	6,000,000	Sundries	500,000
Investments	4,000,000	Total	12,500,000
Total	12,500,000		

This bank has surplus reserves of $400,000. If this bank buys $1,000,000 Federal bonds its statement would be—

ASSETS		LIABILITIES	
Cash in vault	$100,000	Deposits	$11,000,000
Balance in Federal Reserve	2,400,000	Capital stock and surplus	2,000,000
Loans	6,000,000	Sundries	500,000
Investments	4,000,000	Total	13,500,000
Government bonds	1,000,000		
Total	13,500,000		

Surplus reserve is now reduced to $200,000. The only differences would be simultaneous increase in deposit liability in investments of $1,000,000.

And a reduction of the surplus reserves by $200,000—if this bank now received $1,000,000 of interbank currency, its statement would be—

ASSETS		LIABILITIES	
Cash in vault	$100,000	Deposits	$12,000,000
Balance in Federal Reserve	2,400,000	Capital stock and surplus	2,000,000
Loans	6,000,000	Sundries	500,000
Investments	4,000,000	Total	14,500,000
Government bonds	1,000,000		
Interbank currency notes	1,000,000		
Total	14,500,000		

The surplus reserves would remain at $200,000 for its own account. It would hold 100 percent reserve against the new deposits arising from the 1 million interbank currency notes in the form of currency, convertible into lawful money on demand of depositors.

Mr. GOLDSBOROUGH. The first statement is in the usual form. You see that the total assets are $12,500,000 and the total liabilities are $12,500,000. There is a balance there among the assets in the Federal Reserve of $2,400,000 and, on a 20-percent basis, the bank has surplus reserves of $400,000.

Now, in connection with the second statement, we will assume that the bank buys a $1,000,000 Government bond. That adds to its assets a million dollars.

Mr. WILLIAMS. I do not want to interrupt, but I was just wondering where you got the money to buy that bond.

Mr. GOLDSBOROUGH. Maybe we will come to that in just a minute.

That adds to its deposits a million dollars, making the deposits $11,000,000 instead of $10,000,000.

Now, answering Mr. Williams' question, the surplus reserve is now reduced to $200,000. They bought the bond with their deposits, but that reduced the reserve to $200,000.

Mr. WILLIAMS. It seems to me that, according to your statement, your reserves are not reduced. You still have your $2,400,000.

Mr. GOLDSBOROUGH. The cash reserve is the same, but the deposits have been increased, and therefore the surplus reserve is reduced to $200,000.

Mr. WILLIAMS. I do not see the point. I am honest about this, that I do not see the difference. You say that you take a million dollars out of cash, out of reserves, and put that in a bond. You have not added anything there to the liabilities or the assets of the bank at all, have you?

Mr. GOLDSBOROUGH. No; you have not insofar as you and I are concerned, but insofar as the bookkeeping is concerned, you have. That is the way, as I am informed by a bank that I consulted yesterday, that they would fix their books, to show an additional asset and an additional deposit liability.

Mr. WILLIAMS. For instance, you have a million dollars in cash, or in reserves, and you put that into a million-dollar bond. They are both assets. You have simply changed the form of the asset from cash to a bond.

Mr. GOLDSBOROUGH. That is correct.

Mr. WILLIAMS. And that is all that you have done. You have not added anything to either your assets or your liabilities.

Mr. GOLDSBOROUGH. I agree to that, sir; but the fact remains that a bank would add that bond to its assets and would take the deposit which represents the proceeds of that bond and deposit it to the credit of the Government and put it on their books as a liability. That is what they would actually do, so they tell me.

Mr. Williams. I do not see the bookkeeping policy of increasing the assets and liabilities when you have not actually done it.

Mr. Goldsborough. If you want information about bookkeeping, you will have to go to somebody else besides me.

Mr. Williams. Of course, I am no bookkeeper, either, but just as a matter of common sense in connection with the balancing of books, your assets and liabilities, as I see it, and as I understand you agree with me, have been simply changed in form; you have simply changed the form of the assets from cash to a bond.

Mr. Goldsborough. That is right, but when you buy that bond, you reduce your surplus reserve, and it may be that this bookkeeping process is used for the purpose of showing just how your reserves relate to your deposits. I presume that that is the purpose of it, because my attention was called to the fact that when this transaction takes place the surplus reserve is reduced by $200,000. In other words, you have taken a million dollars and used it to buy a bond with, and that has reduced your suplus reserves by 20 percent of a million dollars, so that your surplus reserve is now only $200,000. The cash reserve is still $2,400,000.

Mr. Williams. Let me ask you right in that connection, are you not considering the surplus reserve as part of the assets of the bank?

Mr. Goldsborough. Yes.

Mr. Williams. Then how do you reduce it?

Mr. Goldsborough. You reduce it because you have added to your deposits $1,000,000, from $10,000,000 to $11,000,000, and when you do that, take 20 percent of that $1,000,000, it reduces your cash reserve to $2,200,000.

Mr. Williams. How have you added it to your deposits?

Mr. Goldsborough. It is the proceeds of a Government bond. You simply put a credit on your books in favor of the Government for that much, and let them draw on it. That adds to your deposits.

Mr. Williams. That adds to your deposits, and you also add that bond to your assets.

Mr. Goldsborough. Yes; but that increases your deposits.

Mr. Williams. But you have also taken out of your assets, to start on, $1,000,000 in cash to do it with, and I still come back to where I started, that the books are exactly where they were before the purchase was made, except that you change the form.

Mr. Crawford. May I suggest that it is simply a bookkeeping arrangement here. They give the Government credit for $1,000,000. There is no change of the actual condition, and the minute the Government takes that money, the surplus reserve goes back to where it was before; so really it is a temporary bookkeeping arrangement.

Mr. Williams. But you have not changed the situation in the bank at all.

Mr. Goldsborough. Of course not, but I went to the leading bank in this city to get this statement, and that is how they fixed up their bookkeeping. I have said several times that I am not a bookkeeper.

Mr. Ford. At the time the transaction was consummated, there was actually no money left in the bank at all, in the way of money?

Mr. Goldsborough. That is correct.

Mr. **Ford**. What happened was that the bank purchased from the Government a million dollars worth of bonds. It then went to its deposit liability side—they gave the Government credit for a million-dollar deposit. Later on they received a bond which they put in the assets, to balance it.

Mr. **Goldsborough**. That is correct.

Mr. **Ford**. As a matter of fact, no money changed hands, then, but let us say that tomorrow, after this transaction has been consummated, the bank that bought those bonds is met with a check by the Government on that bank for $1,000,000. That bank would honor that check?

Mr. **Goldsborough**. Yes.

Mr. **Ford**. Then its deposits would be reduced a million dollars, and its reserve would have had to come down proportionately, would it not?

Mr. **Goldsborough**. No.

Mr. **Crawford**. They would go back.

Mr. **Ford**. The reserves would go back proportionately?

Mr. **Goldsborough**. That is correct.

Mr. **Ford**. But this bank would have to have a million dollars right then and there to pay that check.

Mr. **Williams**. What would be the difference whether they paid it today or tomorrow? Suppose that they gave them credit today and paid the cash tomorrow, or suppose that they paid the cash today.

Mr. **Goldsborough**. If the deposit liability was not increased, the surplus reserve would remain the same.

Mr. **Williams**. The result of the transaction is finally that you would be exactly where you started.

Mr. **Goldsborough**. Yes; except that your surplus reserve is reduced.

Mr. **Williams**. I cannot see that.

Mr. **Ford**. There you have a mechanical technicality. Mr. Crawford understands that; he is an expert accountant. Let us hear from him.

Mr. **Crawford**. Let us assume for a moment that the bank actually went to the Treasurer of the United States and said, "Now, we want to give you $1,000,000 in currency for this bond that you are going to hand to us." Looking at the first balance sheet, No. 1, the bank does not have a million dollars in cash, so what it would have to do before it could produce the million dollars in cash would be to realize on the balance in the Federal Reserve bank or on loans or on investments in order to secure the million dollars with which to pay the Treasurer. That bank does not want to dispose of cash, but it does want to go along with the Government and purchase a million dollars' worth of bonds, so it says to the Government, "You give me your I O U, and I will give your Treasurer a credit for $1,000,000."

Mr. **Goldsborough**. That is what happens every time.

Mr. **Crawford**. That is exactly what happens; no question about it.

Now, the deposits advance $1,000,000, because the bank credited the Treasurer of the United States for the I O U, which the Treasurer handled through the bank. Therefore the bank does not have to realize on this balance with the Federal Reserve bank, or on loans, or on investments in order to get the power to command control of the I O U from the Treasurer of the United States.

Now, as to statement No. 2, when the Treasurer of the United States begins to draw against that $1,000,000 by individual checks paid to you or me or someone on the P. W. A. or, say, relief, the recipient of that check goes to the bank. If at that moment he demands currency instead of putting that check back into his deposit account, and if he did the latter, the deposit would still remain the same, but if he demands the cash and puts the cash in his pocket and perhaps walks down the street and buys something, and the merchant returns the cash that afternoon and deposits it to his credit, the bank will probably be out of the possession of the cash for 4 hours, or 4 days, or perhaps 4 weeks.

If a man takes the currency and puts it in a can somewhere and withdraws it from circulation, that begins to do things which we do not like to see happen.

So my observation has led me to see that, as we have issued these I O U's from time to time in the last several years, and as the credit was made to the Treasurer of the United States and he drew checks against those credits in the form of deposits made to him by the banks that took the bonds, and the people so handled their transactions that bank deposits have increased tremendously, and in certain centers, for instance, like Chicago, I think it can be established that there has been a constant curve of increase in deposits as we increased the Federal debt.

Mr. Goldsborough. This second statement is a complete illustration of that. It shows that the purchase of Government bonds by the banks actually increases the deposits of the banks, and that is what we are talking about.

Mr. Crawford. But what I was referring to was that after the transactions have been completed through the operation of the consumer, you might say, and in your second balance sheet it only carries the transaction through to the book entry covering the sale and purchase of bonds.

Mr. Goldsborough. That is true, but it is also true that that deposit will remain within a few dollars the same through a long period of time, because if it is taken out of that bank and put in another bank, there will be a corresponding amount put in another bank on deposit, so that these deposit liabilities will remain practically the same throughout the banking system.

However, these first two statements were only used for the purpose of coming up to the third one, which involves the interbank currency. What I wanted to show, first, was that the purchase of Government bonds and the deposit of a million dollars reduced the surplus reserve by $200,000, and left the surplus reserve at $200,000.

Now, then, go down to the third statement. We will say that this law is in operation, and the bank has received a million dollars in interbank currency represented by the amount it has credited its retailers for their discount currency which they have deposited.

Now, if you will notice that statement, it is exactly like the second statement, except that the interbank currency has been added to it by $1,000,000, and that has increased its deposits by $1,000,000, but this last statement still has exactly the same amount of surplus reserve, because under this act the $1,000,000 representing the interbank currency is not used as a reserve at all, and that leaves the bank's ordinary deposits at $11,000,000, which is supported, therefore, by the same reserve as was required in the second statement. That deposit of interbank currency does not have any effect whatever on the ordinary business of the bank. The ordinary business of the bank has been transacted exactly the same as it was before. Its reserve requirements have not been increased. The only thing that has happened is this, that because of the increased business due to the operation of the retail discount, that bank has on deposit a certain credit that it would not otherwise have. But everything else remains exactly as it was in statement No. 2.

Is that clear?

Mr. WILLIAMS. That is perfectly clear, but suppose that you withdraw it? There is a provision on page 6 that this interbank currency, or credit, whichever you want to call it, may be withdrawn. That is the part that I have not been able to understand. Refer to subsection (f) on page 14, which provides for the withdrawal of the interbank currency. That is where I get in trouble.

Mr. GOLDSBOROUGH. It reads:

> Upon receipt of said notice the banks—

This is subsection (f)—

> the banks shall reduce their outstanding credits so as to increase their surplus reserves sufficiently to permit the return of the proportion of the interbank currency notes held by them to the Treasury without impairing their required legal reserves. In carrying out—

This is surplusage, so far as what we are talking about now is concerned.

> In carrying out the provisions of this section the banks shall promote an orderly liquidation and shall not use selective methods which would tend to depreciate any special classes of securities such as those of the Federal, State, and municipal authorities, and the bond and stock markets, except with the concurrence of the Secretary of the Treasury.

Now, there was a slip handed to each member of the committee the other day which suggested an amendment right there, adding this language:

> On receipt of said notice each bank holding any amount of interbank currency shall reduce its outstanding loans and investments so as to permit the return to the Treasury of its proportion of interbank currency notes called in. Such proportion shall correspond to the ratio that the holdings of the said banks bear to the total amount called in.

Now, Mr. Williams, in the suggested amendment, there was also an amendment to section (i) at the end of title III.

Mr. CRAWFORD. You mean to insert section (i)?

Mr. GOLDSBOROUGH. That is right, to insert section (i), a new paragraph (i) at the end of title III. I have enough copies of this amendment to pass it around again. That reads this way, Mr. Williams:

> It is further provided that nothing in this bill shall be interpreted to destroy such ownership as the banks may have acquired in the interbank currency notes previously held by them, when or if they are recalled by the Secretary of the Treasury on the advice of the Federal Credit Commission as previously provided. When such notes are so recalled the Secretary of the Treasury shall hold them in trust for the benefit of the banks, until such time as the Federal Credit Commission shall advise that they then be returned to the banks which previously held them.

The sole purpose of that, Mr. Williams, is this, that in drawing this bill I made an effort not to interfere in any way that could be avoided with the present banking structure.

Now, my interpretation of section (f), taken in connection with the new section (i), is this, that if an inflation should be caused by this interbank currency, it can be taken out of circulation temporarily until by the operation of the Federal Reserve System, their open-market operations or increased reserves, this inflationary condition shall be corrected. As I interpret subsection (f) and section (i) taken together, they mean that the bank shall not lose its title to this interbank currency, but shall simply temporarily lose the power to use it for banking purposes. That is what it is intended to mean.

Mr. **Crawford**. May I ask a question there?

Mr. Goldsborough, assuming that that actually happened, and that this money was called in and the bank retained its claim, how would that claim be reflected in the published statements and balance sheets of the bank, and would that in turn affect your reserves in any manner? Have you carried that through in the form of an entry?

Mr. **Goldsborough**. I have not carried that through in the form of an entry, but if you will again examine this statement, you will find that this interbank currency, representing, as it does, solely additional business transacted because of the retail discount, does not affect in any way the bank statement, provided that this retail discount was not in operation. It does not effect the ordinary business of the bank at all. It neither increases nor decreases it.

Mr. **Crawford**. On your balance sheet, you would probably show a claim against the fund instead of an interbank currency item of $1,000,000?

Mr. **Goldsborough**. Yes.

Mr. **Williams**. It would still show up as an asset?

Mr. **Goldsborough**. Yes.

Mr. **Williams**. And as a claim against the Treasury of the United States?

Mr. **Goldsborough**. Yes.

Mr. **Williams**. Is it not the hope that finally all of this credit and interbank currency will be eliminated, if you can get retail business so that the consuming public is enabled to consume all of the goods produced in the country, and then the necessity for the use of this interbank currency will pass out?

Mr. **Goldsborough**. Pass out entirely.

Mr. **Williams**. When that time comes, what are you going to do about your bank statement?

Mr. **Goldsborough**. You just would not have the interbank currency on your bank statement any longer.

Mr. **Williams**. Would you have a credit for that anywhere?

Mr. **Goldsborough**. Not if it had passed out.

Mr. **Williams**. You would undoubtedly then have a deficit in your bank account or in your assets of the bank.

Mr. **Goldsborough**. I cannot see that, sir.

Mr. **Williams**. Well, you have a credit, or interbank currency, to make up the deficit——

Mr. **Goldsborough** (interposing). Suppose that the time should come——

Mr. **Williams** (continuing). Let me ask my question, please, for I think that I am entirely muddled on this. You have to have either the interbank currency or a credit with the Treasury—I do not care which you call it—to balance your books.

Mr. GOLDSBOROUGH. Yes.

Mr. WILLIAMS. That is, you have to have that additional asset put on your bank books in order to make up the deficit created by extending credit to the retailer.

Mr. GOLDSBOROUGH. Yes.

Mr. WILLIAMS. That I think is perfectly plain—it is to me. That is the way it looks to me, at any rate. But now, when the time finally comes when all of your interbank currency is retired, and your Treasury credits are wiped out, what will make up that deficit?

Mr. GOLDSBOROUGH. I believe that I can clear that up. The thing which it seems to me would be the best to do, and one of the things which I had in mind in drawing this bill, is that at some time that interbank currency would be purchased by the Treasury, and that the Treasury would give in exchange for it real money, Treasury notes, and that those notes would become demand deposits to take the place of the deposits set up at the time the retailers made their deposits, and that the Federal Reserve System would increase bank reserves in order to prevent an inflation due to the new currency put into circulation, so as to maintain that balance, and that gradually—long in the future—as this real money took the place of the interbank currency and went into circulation, we could gradually reach the point where a 100-percent reserve could be required and still leave ample money in circulation in the form of demand bank deposits to take care of the business of the country, and when that time comes, if it ever comes, the banking business would not be interfered with, because the banks would have the same amount of demand deposits and loans that they always had.

The only difference would be that those demand bank deposits would be supported by 100-percent money rather than fractional money, and it could not interfere with the business of the banks in any way unless it was not quite as necessary for people to borrow as it had been before.

Mr. WILLIAMS. You say that the Treasury will purchase this interbank currency ultimately?

Mr. GOLDSBOROUGH. Yes, sir.

Mr. WILLIAMS. With real money?

Mr. GOLDSBOROUGH. Yes, sir.

Mr. WILLIAMS. Then, after all, you get back to the fundamental proposition, to my mind, in this case, that the Treasury of the United States, the Government, is back of all this, and it is simply a subsidy to that extent.

Mr. GOLDSBOROUGH. I think "subsidy" is a good word but the claim of the proponents of the measure, whether they are right or wrong, is that society is subsidizing itself.

Mr. WILLIAMS. Leaving out the consideration of whatever benefit may be derived from it, the obligation of the United States Treasury is back of it?

Mr. GOLDSBOROUGH. There is no question about that.

Can I go on just a little further?

Mr. WILLIAMS. Of course, that being true, then there is no question but what your books can be balanced, if you furnish money or credit to the extent of the interbank currency.

Mr. GOLDSBOROUGH. Yes.

Mr. WILLIAMS. That will balance the bank books of the country, if the obligation of the Government, to that extent, is called on to pay the difference.

Mr. GOLDSBOROUGH. There is no doubt about it, sir. Now, then, let us assume that through the years this interbank currency increases, making it decreasingly necessary for the fractional reserve system to carry on as it now does; in other words, making it continuously more possible to increase reserves without causing deflation, and let us assume that the time finally arrives when the banks are on a 100 percent reserve basis.

When that time arrives, if you are going to continue to put this money in at the bottom, after that takes place then there is only one way after that for you to get the money and put it in at the bottom, and that is through taxation. When that time comes, you cannot do it by increasing the bank reserves; you will have to do it by taxation.

Mr. WILLIAMS. How much actual money, legal tender, do you think that it would take to transact the business of the country, leaving out bank credit?

Mr. GOLDSBOROUGH. Well, I do not think that you can do without bank credit; I do not see how you possibly can, because people will always have to borrow money. My imagination does not take me to a period when people won't have to borrow money, but under the provisions of this bill, the money needed for the operation of this retail discount could be secured by having the interbank currency gradually increase and at the same time reserve requirements increased, so that there would be absolutely no demand upon the Treasury whatever until the 100 percent reserve point was reached, and when that was reached, then, not being able to increase reserves any more, if you desired to continue with your credit discounts and your interbank currency, then you would have to get it through taxation.

Mr. SPENCE. In your last example, your desposits are $12,000,000 and the balance in the Federal Reserve is $2,400,000. Now, in ascertaining your required reserves, you would subtract that $1,000,000 in interbank currency from $12,000,000, which makes $11,000,000?

Mr. GOLDSBOROUGH. Yes, sir.

Mr. SPENCE. So as you say, the excess reserves would remain at $200,000?

Mr. GOLDSBOROUGH. Yes.

Mr. SPENCE. You say you would hold 100 percent reserve against the new deposits arising from the 1 million interbank currency notes in the form of currency, convertible into lawful money on demand of depositors. Is it the idea that the interbank currency itself will operate as its own reserve, and that the bank would have to retain it?

Mr. GOLDSBOROUGH. It would simply constitute a deposit which could not be loaned out at all.

Mr. SPENCE. But the bank would retain possession of it?

Mr. GOLDSBOROUGH. It would retain the ownership of it.

Mr. SPENCE. Wouldn't that be a rather revolutionary thing, to give a bank control over the reserve itself? At the present time the Federal Reserve bank has control of the reserves. Here the bank itself would have control of its own reserves.

Mr. GOLDSOBOROUGH. No. The word "reserve" is used, but it simply would own that deposit. Of course, if the depositors demanded this interbank currency, they could get it; that is, they could get the money, and the Treasury would have to furnish the money.

Mr. SPENCE. The bank could part with the interbank currency to some other bank, as it could any other currency?

Mr. GOLDSBOROUGH. Yes.

Mr. SPENCE. Then you would give the bank the control over its own reserves, and another independent organization would not have control of them? Wouldn't that be true?

Mr. GOLDSBOROUGH. It would have control of that much more real money which, however, it could not use as a reserve. It would still have to maintain its reserves as it always had.

Mr. SPENCE. My point is that the bank would have physical possession and control of its own reserves, and that is contrary to the general theory of reserves, because reserves are deposited in some independent bank over which the first bank has no control.

Mr. GOLDSBOROUGH. Instead of calling it 100 percent reserve, we can simply call it 100 percent interbank currency—just use different language, and all it would mean is this, that this interbank currency would be segregated from the balance of the bank's business.

Mr. SPENCE. So it would not be a reserve? It would just be segregated in the bank?

Mr. GOLDSBOROUGH. That is what would have to happen to it, and it would not cost the Federal Government one dollar to maintain this retail discount, just as long as it remained possible for the Federal Reserve System to increase bank reserves in order to take in enough money to compensate for the additional currency which had been put into circulation by means of this interbank currency.

Now, of course, if the time should ever come that the banks could be put on a 100 percent reserve basis, then if and when it was necessary to put money into the bottom—and when that time comes they ought not to use interbank currency at all—they ought to use real money when the time came to put that money in at the bottom; in other words, by the exercise of this retail discount, you would have to get that subsidy through a process of taxation. You could not get it in any other way.

But I think it is important to call the committee's attention to the fact that this subsidy, if that is a proper name for it, is a subsidy to all of society. If the bill operates, all that it does is to increase the amount of goods which we can get to all of our people. It is not a subsidy to any one class; whereas we are now granting all sorts of subsidies. We have a subsidy in favor of the poor, in our graduated income tax, and, of course, I am in favor of it, but I mean that it is some kind of a subsidy. It is a subsidy. We have that in our excess-profits tax, and that sort of legislation is not emergency legislation. It is in the permanent law, and intended to remain in the permanent law, and it seems to me that, as far as I can tell, it is certainly the permanent policy of the present administration to retain in the law the agricultural subsidy, the crop reduction subsidy, which is a subsidy, of course, to a class. It is likewise perfectly evident that it is the permanent policy of the Government to retain tariff subsidies.

Now, as the proponents of this bill say, whether they are correct or incorrect, what this legislation does, if the word "subsidy" is to be used, is to subsidize all of society by increasing the amount of goods and services that the people want, increasing the power of the Government to get those things to them.

It was suggested, I think, once by Mr. Ford, and I do not know whether he exactly meant what I understood him to mean or not, but he indicated that this was a subsidy to people who were not able to make purchases. Well, now, is that so? If this act went into operation, J. P. Morgan would get the same reduction on a loaf of bread that he purchased as the servant girl. But you say it is a subsidy to the servant girl, because Morgan does not need the subsidy, and therefore you are giving him something he does not want, whereas you are giving the servant girl something she does want, and therefore it is subsidizing her rather than him.

Well, if you want to use that argument, you can use it now before this legislation, if it is ever passed, goes into operation. You can say now that when they authorize a reduction in prices, those that need it most are being subsidized. You can say that when an automobile is reduced in price from $1,100 to $800, and it makes it possible for the head of a family who could not buy that $1,100 automobile to buy it at $800, that you are subsidizing that class at the expense of the classes of people who could have afforded to buy that automobile at $1,100.

So I just cannot see how the operation of this act, if it acts as the proponents claim that it will act, can constitute a subsidy to any class, and why it won't constitute an addition to the wealth of all classes. That is the argument, as I understand it.

Mr. Gifford. The servant girl gets a subsidy, to be sure, but when it comes to a final subsidy, she probably would not have as much cash as some people, so that one class of society would be subsidizing another. It is not society subsidizing itself.

Mr. Goldsborough. That is the conservative argument; no doubt about that. But I think that there are several answers to it. I think one very obvious answer is that when you find the concealed taxes—and I am going to try to put a list of them into the record; I tried to get it this morning, but I lost my statement, and the girls are looking for it now—when you go through the market basket of the person in very moderate circumstances, I think you will find about 22 percent of the cost of it in concealed taxes of various kinds. I think that that statement is correct, and I think that I can substantiate it.

That is the obvious answer. But, of course, if the proponents of this bill are right in thinking that the actual production of the country can be materially increased by its operation, then all classes will be benefited. If you can increase the production of the country in dollars at present prices from 60 billions to 100 billions, then all of our people are going to get the benefit of that 40 billion dollars of extra production.

Mr. Gifford. Yes; and you encourage production simply by one class of society taking losses. It may be a temporary help to business, but if I want to sell a product at 15 percent less than it cost me, somebody has to make it up to me.

Mr. Goldsborough. Not necessarily at all. It would be so if you were increasing production at one end or if you had production at 100 percent now and then you put a discount on to the ultimate consumer at retail; then somebody would have to pay it—there is not any question about that.

But if you are not able to produce at 100 percent, and if this discount results in increased production equal to the amount of the discount, then it does not cost anybody anything, because you have goods to match your additional dollars that it cost to put this thing into operation. It does not cost anybody anything.

Then there is another consideration, Mr. Gifford, I think, and that is this: That this whole bill is built up on the theory that it does not interfere with the ordinary processes of banking, finance, or industry. As long as the ordinary processes are able to keep the production up and get it to the people for consumption, it does not operate at all, but when they fail, as they have failed ever since I have been born, and according to history, through all time before that—when they do fail, and sometimes fail to such an extent that half of our people, unless they have been fed by society, are to starve, then a process like this would come into operation and save the situation.

Mr. GIFFORD. You strain it down to the breaking point when you say that society as a whole would be greatly benefited. Everybody knows that a tremendous amount of business might be done and 15 percent is a lot of money to grant as a gift. I cannot visualize the amount of money that would be created by a 15-percent discount. It would be a tremendous amount, and when the man who sells you the goods wants his 15 percent from the banks, he will get lawful money, and that lawful money has to be provided by the Treasury of the United States, without question.

Mr. GOLDSBOROUGH. Of course, Mr. Gifford——

Mr. GIFFORD. I do not see any process there of cancelation of that interbank currency. It has got to accumulate, and it is there in the bank to the credit of the man who sells the goods, and the Treasury can call it in whenever it wants to, but the man who sells the goods can demand that his credit be paid to him.

Mr. GOLDSBOROUGH. Mr. Gifford, of course if you are going to assume that everybody who has a bank deposit is going to want cash, why, this system would not operate effectually any more than the present system operates effectually.

Mr. GIFFORD. But your bill says that that 15-percent credit will be placed right to his credit as a deposit, and he can use it.

Mr. GOLDSBOROUGH. Certainly. He can use it by check.

Mr. GIFFORD. I am not lacking in the suspicion that finally that kind of money could be brought around in a circulation scheme, when it could be reloaned.

Mr. GOLDSBOROUGH. Oh, no.

Mr. GIFFORD. I cannot see why it could not be interchangeable. People could swap it around.

Mr. GOLDSBOROUGH. Oh, no.

Mr. GIFFORD. I myself, if I got the 15-percent credit at the bank, could loan you $10 of it as a regular loan, if I could spare it.

Mr. GOLDSBOROUGH. If your deposit increased, and your neighbor's deposit increased——

Mr. GIFFORD. I am simply getting at the segregation of it.

Mr. GOLDSBOROUGH. I will get at it, too, in a minute. If your deposit increases, and your neighbor's deposit increased, it might very readily be that instead of the country being on an installment-plan basis, it might get on a very different basis. It might very readily be that the man who wanted a home would not have to borrow 90 percent from the bank and have the loan insured by the Federal Government.

Mr. GIFFORD. Don't you think that, when interbank currency got to be plentiful, a man who is in business might in some way get it and then loan it right out as a direct loan? If I loaned you $10 out of my deposit, how would the bank determine what kind of money I loaned you?

Mr. GOLDSBOROUGH. It is not the purpose——

Mr. GIFFORD. I know it is not.

Mr. GOLDSBOROUGH. Wait a minute——

Mr. GIFFORD. It is a hard job to see what might not happen under this.

Mr. GOLDSBOROUGH. We cannot both talk at the same time.

Mr. GIFFORD. My imagination is just as good as yours.

Mr. GOLDSBOROUGH. I really do not follow you. A bank deposit would be a bank deposit under the operation of this bill, just like it is now, and would be used just like it is now, and I just don't follow what you have in mind.

Mr. GIFFORD. As you say, it will be exactly as it is now, and if I want to extend a direct loan to somebody for $100, how are they going to know which I draw?

Mr. HARVEY. Might I say a word in explanation?

Mr. GOLDSBOROUGH. Exactly.

Mr. HARVEY. Mr. Gifford, if you look at the bill, you will see that the interbank currency circulation is confined to the banks. It cannot get out into the hands of the public, and that is the reason why that provision was put in, to keep it from getting into the hands of the public in the same way lawful money would. It becomes a form of bank credit. It never gets out into the hands of the public in the form of cash. The banks carry 1 percent of cash in their vaults in order to meet the demands——

Mr. GIFFORD. But supposing the man goes in and demands cash, and gets it; then are you hemmed in for the purpose of using it after you get the cash?

Mr. HARVEY. If the cash is demanded, but there are 50 billions of deposits in the banks for which the banks are liable, and there are 10 billions of deposits in the banks for which the Government is liable. The demand for cash will then be 5 to 1 as far as the Government is concerned, and the Government will have to make the 10 billion dollars good against the banks having to make the 50 billion dollars good.

Now, at the present time the banks cannot make that 50 billions in deposits good; they never have been able to do it, so that the obligation of the Government to pay legal tender currency is only at the present moment, if we visualize this interbank currency in the banks as deposits, one-fifth or one-sixth of the total that the banks will be liable for in the form of legal-tender currency.

Mr. GIFFORD. Mr. Goldsborough said that the deposits of these discounts would be credited to the individual just the same as anything else, and then the individual can draw a check on them.

Mr. HARVEY. He draws a check on his deposit, but not on the interbank currency.

Mr. GIFFORD. That is not what Mr. Goldsborough said.

Mr. GOLDSBOROUGH. That is exactly what I said. There is no difference at all between what Mr. Harvey said and what I said.

Mr. GIFFORD. If there is no difference, then I will draw that check and let you have the $10.

Mr. GOLDSBOROUGH. I will take your check whenever you see fit to draw it.

Mr. TRANSUE. The question that is bothering me about this bill is this—and probably you can clear it up—whether or not the banks, if they kept giving this 15-percent discount, or credit to the retail merchants, would not soon have a great deal of their deposits and their surplus and capital invested in interbank currency?

Mr. GOLDSBOROUGH. I am not sure that I understand the purport of your question.

Mr. TRANSUE. Well, if I can explain a little more fully, a man goes to the bank day after day with his receipts and gives his discount paper, and he is given a deposit credit for the 15 percent of the amount that he deposits, which becomes a liability of the bank, to give him the right to draw a check or to give him cash, and then in turn the bank gets interbank currency for it. Now, as that keeps on, the banks would soon have a great deal of this interbank currency in their vaults, in their portfolios, it seems to me. Is that right or not?

Mr. GOLDSBOROUGH. Well, I do not know whether you were in here when this began this morning or not.

Mr. TRANSUE. No, I was not.

Mr. GOLDSBOROUGH. We went over all that.

Mr. TRANSUE. Excuse me.

Mr. GOLDSBOROUGH. That is all right.

Mr. CRAWFORD. May I ask Mr. Goldsborough a question?

Mr. GOLDSBOROUGH. I will answer you in a minute, Mr. Transue.

Mr. CRAWFORD. Do you want to answer his question?

Mr. GOLDSBOROUGH. I thought you wanted to make an observation in regard to his question.

Mr. CRAWFORD. I want to touch on this.

The CHAIRMAN. Finish with Mr. Transue.

Mr. GOLDSBOROUGH. We went over that this morning, sir, and the way this law would operate, so the proponents of it think, would be that as interbank currency increased in the banks, the Federal Reserve Board would raise the reserve requirements so as to prevent an inflation, and as this interbank currency took the place of the money loaned by the banks and redeposited on a fractional reserve basis, the reserve requirement would have to increase, and ultimately the reserve requirement would be 100 percent, because there would be enough of the interbank currency to transact the business of the country without using a fractional reserve system, and it is anticipated that from time to time there would be legislation which would convert a whole or a part of the interbank currency to real money by requiring the Treasury to exchange Treasury notes for interbank currency.

It was argued this morning by me that until the Federal Reserve System had exhausted its right to increase the reserves of the banks, this retail discount could operate without costing the Federal Treasury a single cent, and that when that time arrived, the banks would be doing business on the basis of a 100-percent reserve. It would then be necessary, in order to put money in the bottom through this retail discount, to resort to taxation in order to get the money to do it. That was my contention. I do not know whether I made it clear to you or not.

Mr. **Transue.** I heard you say that, and it probably should be clear to me, but I am sorry to say that it still is not.

Mr. **Crawford.** Mr. Goldsborough, all through these hearings, it seems to me that we have incorrectly built up the record in this respect, that almost every day we have been referring to a 15-percent discount. Now, as I understand this bill, it in no place refers to a 15-percent discount on goods to be granted at any time, but in subsection (c) of section 4, it does mention a 15-percent discount, but not as related to a discount, and the figure it does relate to as a discount if 5 percent, in graduated amounts of only 5 percent.

Have we not been incorrect in referring to the 15-percent discount all along?

Mr. **Goldsborough.** Why, Mr Crawford, the bill does provide for an initial discount of 15 per cent.

Mr. **Crawford.** In what section is that? If so, I have overlooked it.

Look at page 4, subsection (c), section 4.

Mr. **Ford.** It is section (b) on page 3, and it says that—

> Upon the passage of this act and until the retail discount rate is determined and proclaimed as above provided, the retail discount rate shall be 15 per centum

Mr. **Goldsborough.** The initial discount, Mr. Crawford, is 15 percent, but the Federal Credit Commission cannot change the discount from one amount to another by more than 5 percent.

Mr. **Crawford.** The bill also provides, however, that it is simply an initial discount?

Mr. **Goldsborough.** That is an initial discount, and it provides——

Mr. **Crawford** (interposing). Would you go so far as to say that after the establishment of a retail discount, by the mechanics of the bill the 5 percent mentioned in subsection (c) of section 4 shall be added to that initial 15 percent?

Mr. **Goldsborough.** Well, it would be this way: If it was found that the difference between what could be produced of wanted goods and services and what was being consumed was as much as 35 percent—if that was the difference—then the Federal Credit Commission could increase the discount 5 percent from time to time up to 20 percent. There is to be a gap in order to prevent inflation between production and consumption, of 15 percent. If they found that the actual gap was 35 percent, they could make the discount 20 percent.

Mr. **Crawford.** Within a period of 4 months?

Mr. **Goldsborough.** Within a period of 4 months, yes.

Mr. **Crawford.** So, then, coming back to my original question, are we not in error when we seem to anchor this thing down to 15 percent?

Mr. **Goldsborough.** Well, the 15 percent discount, of course, as you say, is only an initial discount, to be used for experimental purposes.

Mr. **Crawford.** That is what I wanted to get clear in my mind.

Mr. **Goldsborough.** And the discount would go up and down. The proponents of the bill are of the opinion that as the financial, the banking, and the industrial structure of the country would know that this cushion, the discount, would always be available in case of a business recession, it would restore confidence so that the discount would very seldom have to be used after it once gets into operation. That is the hope and the anticipation of the proponents of the bill.

Mr. Crawford. Just one more question. Referring to lines 1 to 3, on page 4 of the bill——

Mr. Goldsborough (interposing). Yes.

Mr. Crawford. What relation does that language have to line 8 on page 4 of the bill, because, as I read that, lines 1 to 3 determine what the retail discount shall be after the initial stage has passed.

Mr. Goldsborough. Well, of course, there had to be some figure used as an initial figure. If after the operation of the bill for 4 months, we will say, we find that there has been a rise in prices, indicating that production had approached consumption so that there was a gap between production and consumption of less than 15 percent, you would have to take off the discount entirely.

Mr. Williams. Let me see if I understand that. Are you through, Mr. Crawford?

Mr. Crawford. Yes.

Mr. Williams. In one place in the bill, as I read it, it seems, to me at least, that the retail discount is determined by the unused productive capacity.

Mr. Goldsborough. That is right.

Mr. Williams. And in another place it is determined—and whether there is any difference in it or not, I do not know—by the difference between the productive and consumptive capacities.

Mr. Goldsborough. Well, probably in the first instance, Mr. Williams, in writing the bill, it was assumed that the people could consume all that they could produce. Now, the idea is to increase production to within 15 percent of the amount of wanted goods and services that the people can consume, things that they want.

Mr. Williams. The expression "wanted goods and services" has been used all through here. That is another expression that I do not know the meaning of. Is that a static situation?

Mr. Goldsborough. My Lord, no.

Mr. Williams. Or progressive?

Mr. Goldsborough. Anything else but a static one, I should say.

Mr. Williams. Well, then, that means that as conditions improved, the wants will increase?

Mr. Goldsborough. Inevitably.

Mr. Williams. And the further you go, the more you consume, the more you produce?

Mr. Goldsborough. Yes; that is what it means.

Mr. Williams. It is a continual increase, not only of production, but of consumption also?

Mr. Goldsborough. That has been our theory. Nobody has ever been able to satisfy human want. The more people get, the more they want, and that is inevitable.

Mr. Williams. We would have to improve our productive capacity a great deal, would we not?

Mr. Goldsborough. We would not for a long time.

Mr. Williams. To supply all needed wants?

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Mr. Goldsborough. We would not for a long time, but, you know, in talking with industrialists, I find that there are a great many suppressed inventions that they are not using, because they do not want production increased. They would not want this stuff if it was increased.

Mr. Williams. It strikes me that if we produced everything that everybody wants, in a general sense, there would be a very big increase in production, if we met that demand.

Mr. Goldsborough. I hope so, because I believe that the bank deposits of the country and the status of the wealth of the country indicate that not over 1 or 2 percent of the people really feel that they are out of the woods, that they are not in danger of poverty in their old age.

Mr. Spence. Would not the facts that the Federal Credit Commission would have to ascertain be highly controversial?

Mr. Goldsborough. No, I do not think so. I have talked very extensively with men connected with the Brookings Institution, and I am fully convinced that, aside from the Brookings Institution, the Department of Agriculture and the Department of Commerce could come within a percent that is very small.

Mr. Spence. Do you think we can find anywhere in the world—and I say this with all seriousness—4 experts out of 7 that would agree on anything? That has not been our experience.

Mr. Goldsborough. This is a factual matter. Factual matter I think they agree upon pretty well, but where they do not agree is in the realm of theory. One of them will say that the Federal Reserve Board ought to have done one thing to restore confidence, and the next man will say that if they had done something else that confidence would have been restored, but that is nothing but the realm of conjecture, but I think that when it comes into factual matter, something that they can touch with their fingers, they agree very well.

(Thereupon, at 12:10 p. m., the committee adjourned to meet again Monday, March 14, 1938, at 10:30 a. m., to consider another bill.)

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